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In the

Supreme Court of the United States

October Term, 1983

CENTRAL STATES, SOUTHEAST AND SOUTHWEST AREAS PENSION FUND and CENTRAL STATES, SOUTHEAST AND SOUTHWEST AREAS HEALTH AND WELFARE FUND,
Petitioners,

v.

CENTRAL TRANSPORT, INC., et al.,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

PETITIONERS' BRIEF ON THE MERITS

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QUESTION PRESENTED

In implementing a field audit program in accordance with the "prudent man" rule of ERISA, may the trustees of multiemployer employee benefit funds, without being arbitrary or capricious, request access to payroll, tax, and other "pertinent records" relating to the wages, hours and duties of *all* employees of contributing employers:

1) Where the purpose of the audit is to monitor a self-reporting system and to assure compliance with statutory and contractual obligations;

2) Where the funds must award service credits and benefits to employees on the basis of work performed under a collective bargaining agreement even in the absence of employer contributions;

3) Where records relating to an employer's complete work force are necessary to comply with generally accepted auditing standards;

4) Where substantial safeguards are offered to protect the confidentiality of employee records;

5) Where the trust agreements governing the funds, as construed by the trustees, authorize such audits;

6) Where, absent such audits, the trustees must rely on the discretionary efforts of unions, employees, or the Secretary of Labor to oversee employer contributions and hence to protect the actuarial solvency of the funds.

OR

May employers withhold the records of all employees except those they *concede* are covered by the collective bargaining agreement *unless* the trustees first established reasonable cause to believe that other individuals perform bargaining unit work and should be reported regardless of how the employer has classified them?

LIST OF RESPONDENTS

Respondents, collectively styled Central Transport, are: Central Transport, Inc., Central Cartage Co., Quad State Leasing, Inc., Cadillac Leasing, Inc., Dunes Leasing, Central Recapping Inc., Michiana Trucking, Inc., Company 17, Danville Illinois Leasing, Michigan Express, Mohawk Cartage, Mohawk Motor, Inc., Flint Cartage, Bancroft Freight Lines, and McKinlay Transport, Ltd. Central States originally filed suit also against Genessee Cartage; this company was omitted from the appeal.

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
LIST OF RESPONDENTS	ii
TABLE OF CONTENTS	iii
TABLE OF AUTHORITIES	v
OPINIONS BELOW	1
JURISDICTION	1
STATUTES INVOLVED	2
PETITIONERS' STATEMENT OF THE CASE	2
1. Introduction	2
2. The audit of Central Transport	6
3. Statutory context	9
4. Central States' audits and their function	12
5. Proceedings below	16
SUMMARY OF ARGUMENT	18
ARGUMENT	23
I. ERISA PERMITS TRUSTEES OF MULTI-EMPLOYER PLANS TO CONDUCT RANDOM GENERAL AUDITS TO VERIFY THE ACCURACY OF REPORTING AND TO IDENTIFY ALL ELIGIBLE PLAN PARTICIPANTS	23
I.A. Random general audits are "prudent" within the meaning of 29 U.S.C. § 1104	23
I.A.1. Trustees have express and implied powers under ERISA as under the common law; the right to audit is an implied power	23
I.A.2. Access to complete records is necessary for a genuine and independent audit given a self-reporting system: the IRS and Fair Labor Standards Act analogies	27
I.A.3. Post-ERISA case law illustrates why audits limited to the records only of concededly covered employees would endanger fund assets and hence be imprudent	31

TABLE OF CONTENTS—(Cont'd)

Page

I.B. Prudence dictates that fund trustees develop independent methods for monitoring employer compliance: reliance on third persons is inconsistent with the spirit of ERISA, the LMRA, and case law 37

I.C. Prudence dictates that the Central States Trustees maintain a vigorous field-audit program as an "internal control" which is relied upon by its independent CPA in certifying the Funds' annual financial reports 40

II. THE TRUSTEES' NEED FOR INFORMATION OUTWEIGHS THE EMPLOYER'S INTEREST IN CONFIDENTIALITY: A REVIEW OF THIS DEFENSE TO DISCLOSURE IS AS NECESSARY IN THE CONTEXT OF ERISA AS IT WAS IN THE CONTEXT OF THE NATIONAL LABOR RELATIONS ACT 43

III. THE TRUST AGREEMENTS GOVERNING THE CENTRAL STATES FUNDS PROVIDE A CONTRACTUAL BASIS FOR RANDOM GENERAL AUDITS 46

CONCLUSION 48

APPENDIX ..... A-1—A-13

TABLE OF AUTHORITIES

Cases: Page

Adams v. *N.J. Brewery Employees Pension Trust Fund, et al.*, 670 F.2d 387 (3d Cir. 1982) 42

Audit Services, Inc. v. *Rolfson*, 641 F.2d 757 (9th Cir. 1981) 34

Barrentine v. *Arkansas-Best Freight System*, 450 U.S. 728 (1981) 38

Brick Masons Pension Trust v. *F.K. Pullen*, 113 L.R.R.M. 3040 (C.D. Cal. 1983) 33

Brogan v. *Swanson Painting Co.*, 682 F.2d 807 (9th Cir. 1982) 34

Bugher v. *Consolidated X-Ray Service Corp.*, 705 F.2d 1426 (5th Cir. 1983) 20

Central States, Southeast and Southwest Areas Pension Fund v. *CRST*, 641 F.2d 616 (8th Cir. 1981) . 23

Central States, Southeast and Southwest Areas Pension Fund, et al. v. *Howard Martin*, 625 F.2d 171 (7th Cir. 1980) 31

Central States, Southeast and Southwest Areas Pension Fund, et al. v. *Hribar Trucking Co.*, No. 81-2422 (7th Cir. June 16, 1982) 41

Central States, Southeast and Southwest Areas Pension Fund v. *Theut Products, Inc.*, No. 82-71080 (E.D. Mich. 1982) 15, 31

Cudahy Packing Co. v. *Fleming*, 122 F.2d 1005 (8th Cir. 1941), *rev'd (on other grounds)*, 315 U.S. 785 (1942) 30

Curtiss-Wright v. *NLRB*, 59 L.R.R.M. 2433 (3rd Cir. 1965) 44

Danti v. *Lewis*, 312 F.2d 345 (D.C. Cir. 1962) 42

Donaldson v. *U.S.*, 400 U.S. 517 (1971) 43

Fleming v. *Montgomery Ward Co.*, 114 F.2d 384 (7th Cir. 1940), *cert. denied*, 61 S. Ct. 71 (1940) 20, 30

TABLE OF AUTHORITIES—(Cont'd)

Cases: Page

Jim McNeff v. *Todd*, ____ U.S. ____, 103 S. Ct. 1753 (1983) 20, 31

Johnson v. *Botica*, 537 F.2d 930 (7th Cir. 1976) 36

Kemmis v. *McGoldrick*, 706 F.2d 993 (9th Cir. 1983) 34

Kosty v. *Lewis*, 319 F.2d 744 (D.C. Cir. 1963) 24

Laborers Health and Welfare Trust Fund, et al. v. *Kaufman and Broad*, 707 F.2d 412 (9th Cir. 1983) 20, 33

Maness v. *Williams*, 513 F.2d 1264 (8th Cir. 1975) .. 42

Manning v. *Wiscombe*, 498 F.2d 1311 (10th Cir. 1974) 34

Marsh v. *Greyhound Lines, Inc.*, 488 F.2d 278 (5th Cir. 1974) 42

Nachman Corp. v. *PBGC*, 446 U.S. 359 (1980) 10

Nedd v. *United Mine Workers of America*, 556 F.2d 190 (3d Cir. 1977), on remand, 506 F.Supp. 891 (M.D. Pa. 1981) 36

Nichols v. *Trustees of Asbestos Workers Local 24 Pension Plan*, 3 EBC 1726 (D.D.C. 1982) 21, 35, 36, 43

NLRB v. *Acme Industrial Co.*, 385 U.S. 432 (1967) . 45

NLRB v. *Amax Coal Co.*, 453 U.S. 322 (1981) 21, 24, 46

NLRB v. *Detroit Edison*, 440 U.S. 301 (1979) 45

Oklahoma Press Publishing Co. v. *Walling*, 327 U.S. 186 (1946) 20, 30

Pacific Iron & Metal Co. v. *Western Conference of Teamsters Pension Trust Fund*, 553 F. Supp. 523 (W.D. Wash. 1982) 39

PBGC v. *R.A. Gray & Co.*, 52 U.S.L.W. 4810 (U.S. June 18, 1984) (No. 83-245) 10

TABLE OF AUTHORITIES—(Cont'd)

Cases: Page

Pete v. *United Mine Workers*, 517 F.2d 1275 (D.C. Cir. 1975) 36

Rehmar v. *Smith*, 555 F.2d 1362 (9th Cir. 1976) 42

Riley v. *MEBA Pension Trust*, 570 F. 2d 406 (2d Cir. 1977) 48

Robbins, et al. v. *Prosser's Moving and Storage Co.* and *Robbins, et al.* v. *Schneider Moving and Storage Co.*, 700 F.2d 433 (8th Cir. *en banc* 1983), *aff'd sub nom. Schneider Moving & Storage Co., et al.* v. *Robbins, et al.*, ___ U.S. ___, 104 S. Ct. 1844 (April 18, 1984) (Nos. 82-1860, 82-1862) 21, 22, 23, 24, 31, 32 37, 38, 40, 46, 48

Rosen v. *Hotel and Restaurant Employees, Local 274*, 637 F.2d 592 (3d Cir. 1981), *cert. denied*, 102 S. Ct. 398 (1981) 21, 36, 38, 39

Struble et al. v. *New Jersey Brewery Employees Welfare Trust Fund, et al.*, (No. 83-5115, 5220, 5221, 5222, 5223, 5224) ___ F.2d ___ (3d. Cir. 1984) .. 43

Teamsters Construction Workers Local 13 Health and Welfare Trust Fund v. *Hawg N Action*, 651 F.2d 1384 (10th Cir. 1981) 20, 34, 35

United Mineworkers of America Health and Retirement Funds v. *Robinson*, 455 U.S. 562 (1982) 37

U.S. v. *Arthur Young*, ___ U.S. ___, 104 S.Ct. 1906 (March 21, 1984) (No. 82-687) 42, 43

U.S. v. *Bisceglia*, 420 U.S. 141 (1974) ... 20, 28, 29, 46

U.S. v. *Davey*, 404 F. Supp. 1283 (S.D.N.Y. 1975) . 28

U.S. v. *Powell*, 379 U.S. 48 (1964) 20, 29, 30

U.S. v. *Prince Carpentry Inc. et al.*, 84-188 (E.D.N.Y. March 20, 1984) 14

U.S. v. *S & Vee Cartage*, 704 F.2d 914 (6th Cir. 1983) 1983) 12, 29

TABLE OF AUTHORITIES—(Cont'd)

Cases: Page

Van Gunten v. *Central States, Southeast and Southwest Areas Pension Fund*, 672 F.2d 586 (6th Cir. 1983) 10

Waggoner v. *C & D Pipeline Co.*, 601 F.2d 456 (9th Cir. 1979) 35, 36

Waggoner v. *Dallaire*, 649 F.2d 1362 (9th Cir. 1981) 34

Walsh v. *Schlecht*, 429 U.S. 401 (1977) 20, 34

Wardle v. *Central States, Southeast and Southwest Areas Pension Fund*, 627 F.2d 820 (7th Cir. 1980) (1980) 42, 43

Welfare Fund v. *Overhead Door Co.*, 104 L.R.R.M. 2653 (D.D.C. 1980), *rev'd*, 110 L.R.R.M. 2752 (D.C. Cir. 1982) 33

Statutes:

Fair Labor Standards Act, 29 U.S.C. § 211 .... 6, 30, 39

Labor Management Relations Act,

29 U.S.C. § 158(a)(5) (Sec. 8(a)(5)) 44

29 U.S.C. § 186 (Sec. 302; Sec. 302(c)(5)) ... 3, 34, 37

Employee Retirement Income Security Act,

29 U.S.C. § 1001 ..... 5, 10, 30, 37, 43

29 U.S.C. § 1002(6) 11

29 U.S.C. § 1002(7) 11

29 U.S.C. § 1002(14) 25

29 U.S.C. § 1021 11

29 U.S.C. § 1022 ..... 11, 24, 26

29 U.S.C. § 1023 24

29 U.S.C. § 1024 ..... 11, 24, 26

29 U.S.C. § 1025 ..... 11, 24, 26

29 U.S.C. § 1027 ..... 11, 24

29 U.S.C. § 1052(a)(3)(A)(C) 10

TABLE OF AUTHORITIES—(Cont'd)

Page

29 U.S.C. § 1053(b)(2)(A) 10

29 U.S.C. § 1059 ..... 11, 24

29 U.S.C. § 1102 10

29 U.S.C. § 1103 ..... 9, 10, 25

29 U.S.C. § 1104 ..... 5, 10, 17, 19, 23, 24, 25, 26, 35, 47, 48

29 U.S.C. § 1105 ..... 10, 21, 47

29 U.S.C. § 1106 ..... 24, 25

29 U.S.C. § 1132(b)(2) 40

29 U.S.C. § 1132(g)(2) 25

29 U.S.C. § 1134 39

29 U.S.C. § 1145 ..... 5, 25

29 C.F.R. § 2530.220b-2(a)(1) and (2) 10

29 C.F.R. § 2530.200b-3(a) and (e) 11

Multiemployer Pension Plan Amendments Act,
29 U.S.C. § 1381, *et seq.* 5, 33, 40

Internal Revenue Code
26 U.S.C. § 7601 ..... 6, 28

26 U.S.C. § 7602 ..... 28, 43

Crimes and Criminal Procedure, 18 U.S.C. § 1027 ..... 12, 29

Jurisdictional Statutes:
28 U.S.C. § 1254(1) 2

28 U.S.C. § 1292(a)(1) 2, 16

Miscellaneous:
AICPA, *Statement on Auditing Standards No. 39,* ¶ 17, AU 350.17 41

AICPA, *Audits of Employee Benefit Plans* (1983) ... 40

TABLE OF AUTHORITIES—(Cont'd)

Page

Financial Accounting Standards Board (FASB) Statement No. 35, *"Accounting and Reporting by Defined Benefit Pension Plans"* (March 1980) 40

CCH Fed. Sec. Laws Reports: SEC Accounting Release No. AS-19, ¶ 72,020 15

Bogert, *The Law of Trusts & Trustees*, Chap. 46, *Accounting and Compensation* (rev. 2d ed. 1980) . 23

Bogert, *The Law of Trusts & Trustees*, Chap. 27, *Trustees' Powers in General* (rev. 2d ed. 1980) ... 25

Gilbert, Lachowitz, & Zid, *Accounting and Auditing for Employee Benefit Plans* (Warren, Gorham & Lamont, New York and Boston: 1978) 41

CCH Pension Plan Guide, ¶ 25,496 (May 19, 1983).. 40

3 *U.S. Code Cong. & Ad. News* (1974) 5, 24

House Conf. Rept. 93-1280 (Pub. L. No. 93-406) 5

126 Cong. Rec. (House) 23039 (Aug. 25, 1980) 33, 36

DOL Advisory Opinion Letter 76-89 10

DOL Advisory Opinion Letter 78-28 25

DOL and IRS Reg. 76-1, 41 F.R. 12740 (March 26, 1976) 12, 25

Black's Law Dictionary 27

Webster's New World Dictionary of the American Language 27, 44

Oxford English Dictionary 27, 28, 44

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PETITIONERS' BRIEF ON THE MERITS

OPINIONS BELOW

The district court opinion is reported at 522 F. Supp. 658 and set forth in Appendix A to the Petition for Certiorari (A 1-14).[1] The opinion of the court of appeals is reported at 698 F.2d 802 and set forth in App. B P.C. (A 15-34).

JURISDICTION

The judgment of the court of appeals was entered on January 20, 1983 (App. C P.C., A 35-36). A Petition for Rehearing *en banc* was denied on April 8, 1983 (App. D P.C., A 37). Central States filed its Petition for Certiorari on July 2, 1983. On October 3, 1983, this Court granted

[1] All further references to this Appendix will be indicated by the abbreviation "App. P.C." and the appropriate subsections ("A"-"J") followed by page numbers. Central States' Complaint and audit engagement letter are reprinted as Appendix A and B to this Brief.

leave for three Amici to file Briefs in support of the Petition.[2] On this date, the Court also invited the Solicitor General to express the views of the United States. In May, 1984, the Solicitor General together with the Solicitor of Labor filed a Brief in support of the Petition. The Solicitor General was also authorized to represent that the PBGC concurred in the view that further review was warranted (Sol. Gen. Brief, p. 18, fn. 16). This Court granted Central States' Petition on June 18, 1984. Jurisdiction was invoked under 28 U.S.C. § 1254(1). The court of appeals assumed jurisdiction under 28 U.S.C. § 1292(a)(1); the district court assumed jurisdiction under 29 U.S.C. § 185(a) (LMRA) and 29 U.S.C. § 1132 (ERISA).

STATUTES INVOLVED

The relevant provisions of the National Labor Relations Act, 29 U.S.C. § 151, *et seq.*, as amended by the Labor Management Relations Act of 1947, 29 U.S.C. § 141, *et seq.*, and the Employee Retirement Income Security Act of 1974, 29 U.S.C. § 1001, *et seq.*, as amended by the Multiemployer Pension Plan Amendments Act of 1980 (Pub. L. No. 96-364), are set forth in App. G P.C. (A 50-81).

PETITIONERS' STATEMENT OF THE CASE

1. Introduction

Central Transport, an interstate trucking company, like some 12,000 other employers engaged in transportation and other industries, operates its business pursuant to collective bargaining agreements with Teamster local unions. These agreements require specified weekly contributions to the Central States Health and Welfare and Pension Funds on behalf of each employee who performs bargaining unit work. The Trustees of the Central States Funds are required by ERISA and corresponding regulations to sys-

[2] The National Coordinating Committee for Multiemployer Plans (NCCMP) and the Bricklayers Fringe Benefit Funds—Metropolitan Area et al. (together representing more than 150 Taft-Hartley pension and welfare plans and over 8 million American workers employed in various major industries throughout the United States); and Arthur Young & Co. (a "Big Eight" accounting firm which audits employer records and also multiemployer plans, including Central States).

tematically ascertain and collect all contributions owed by employers under operative collective bargaining agreements. The Trustees of the Pension Fund are also required by law to grant service credit and ultimately benefits to anyone who has performed bargaining unit work regardless of whether the employer has remitted corresponding contributions. Because of its size, Central States, like most multiemployer plans, operates on a self-reporting system. Thus, the Trustees *must* rely on employers to report accurately. Because a significant number of employers do not report or contribute *regularly* on behalf of some eligible employees or *at all* on behalf of others, the Trustees conduct *random* field audits to inspect employer accounts. The specific issue for review is whether, in conducting audits to verify the accuracy of reporting, fund trustees may request access to pertinent records relating to *all* employees in a contributing employer's work force, since it is possible for an employee to perform bargaining unit work but not be reported. Notwithstanding the fact that independent verification of data lies at the heart of generally accepted auditing standards, the court of appeals held that the Trustees may not conduct such *general* audits. Absent *reasonable cause* to believe that a *particular omission* has occurred, the Trustees are *limited* to the records of employees the employer *concedes* are "covered" by the collective bargaining agreement (App. B P.C., A 31-32).

In its opinion, the court of appeals did not address the magnitude of the problem of misreporting to Taft-Hartley trust funds,[3] did not address the function of random general audits as a device to deter as well as to uncover delinquent contributions, did not analyze the role of generally accepted auditing standards in ERISA, did not address the need for trustee independence in the area of audits and collections, and departed from the standard of judicial review traditionally applied by other courts in interpreting trustee decisions under the common law of trusts, which law has been incorporated into the "prudent man" rule of ERISA. Focusing heavily on the cost of audits and on the confidentiality of employee records, rather than on the Trustees' need to obtain verification data independently and to pre-

[3] A "Taft-Hartley" trust is one established and governed in accordance with Section 302(c)(5) of the LMRA.

vent a drain on fund assets, the court restricted the permissible scope of an audit, erected a "reasonable cause" threshold, and thus inhibited the Trustees in the performance of a core fiduciary duty ordained by statute and embodied in relevant contracts. In so doing, the court rejected the Trustees' contention that by limiting the records open to inspection, the *employer*, which has sole and ready possession of the information needed, would control the audit although the Funds, which have no other feasible access to the data, would bear ultimate financial responsibility.

Petitioners are two of the largest trust funds in America. With assets in excess of four billion dollars, the Central States Health and Welfare and Pension Funds serve some 500,000 active workers, retirees, and their families who depend on them for retirement income and health coverage and thus rely on the Trustees to determine and collect contributions, protect fund assets and otherwise assure actuarial solvency. While the court of appeals recognized the need to "correlate" disbursements from and contributions to the Funds, it rejected the *method selected by the Trustees* as the ordinary and natural means for achieving this result in accordance with the broad administrative discretion vested in them by ERISA, the LMRA, the Trust Agreements governing the Funds, and the common law of trusts.

The importance of the Trustees' claim of right to determine the reasonable scope of an audit of contributing employer records and to conduct it in accordance with generally accepted auditing standards as well as the magnitude of the court of appeals' misapprehension of the issue is evidenced by the detailed Briefs filed in support of Central States' position by representative *Amici*, including the Department of Justice and the Department of Labor, with the concurrence of the Pension Benefit Guaranty Corporation.

This is a case of first impression involving an issue of great national importance rather than one seeking resolution of a direct conflict between or among the circuits. While Central States seeks a reexamination of its *contractual* right to conduct the type of audit requested and hence an enunciation of the proper standard for the judicial review of

Trustee interpretations of the Trust Agreements which articulate their powers, Petitioners have a more fundamental request; namely, that this Court give specific content to the "prudent man" rule of ERISA (29 U.S.C. § 1104) as Congress *expressly* envisioned: "The conferees expect that the courts will interpret this prudent man rule (and the other fiduciary standards) bearing in mind the special nature and purpose of employee benefit plans." House Conf. Rept. 93-1280 (Pub. L. No. 93-406), 3 *U.S. Code Cong. & Ad. News* 5083 (1974). To this end, it may be well at the outset to reflect upon Congress's finding that private pension and benefit plans, dedicated to the security and well-being of millions of Americans, are affected with a national public interest impacting interstate commerce and the tax revenues of the United States (29 U.S.C. § 1001); that the financial health of such plans has become ever more important as a result of the increasing fragility of the Social Security system, the escalating costs of medical care, and the increasing life-expectancies of this country's citizens together with an entrepreneurial effort to encourage earlier retirement; that trustee efforts to maximize fund assets through vigorous enforcement of contractual obligations are motivated *solely* by a fiduciary obligation to protect the interests of plan participants and beneficiaries and are not *in any way* directed toward private gain; that most multiemployer plans operate on a self-reporting system analogous to that underlying the federal tax scheme; that Congressional concern with delinquencies led in 1980 to the creation of a new and specific ERISA cause of action where an employer violates the terms of a collective bargaining agreement or a multiemployer plan;[4] and, finally, that Congress chose not to interpose a governmental entity between employers and employees to enforce routine compliance with ERISA but left this task to the Trustees themselves through procedures to be designed by them, pursuant to the "prudent man" rule (29 U.S.C. § 1104), and in accordance with the particular constituency, needs, and circumstances of the plan. Throughout this Brief, Petitioners will therefore view mul-

[4] *See*, Section 306 of the Multiemployer Pension Plan Amendments Act of 1980 (Pub. L. No. 96-364); 29 U.S.C. § 1145 (App. G P.C., A 80). Trustees prevailing in a collection action under this section of ERISA are entitled to the mandatory award of the principal amount of delinquent contributions, interest, statutory damages, and attorney fees.

tiemployer plans as quasi-administrative in nature and trustees as functional equivalents of the Tax Commissioner charged with "canvassing" the United States to "inquire after" and collect any tax due (26 U.S.C. § 7601, *et seq.*) and the Administrator of the Wage and Hour Division of the DOL charged with verifying employer compliance with the Fair Labor Standards Act (29 U.S.C. § 211).

2. The audit of Central Transport

"Central Transport" ("Transport") is the collective name for 16 companies admittedly engaged in or supportive of interstate trucking (*see* p. ii; Appellants Brief, p. 1). Each of these companies was admittedly signatory to the National Master Freight Agreement (NMFA) and one or more of its Supplemental Agreements executed between itself and a Teamster local (App. A P.C., A 3; App. B P.C., A 16). Pursuant to these agreements, Transport was obligated to remit on a monthly basis specified weekly contributions for each employee "covered" by the contract.[5]

The Trust Agreements governing each Fund are incorporated by reference in the respective health and welfare and pension provisions of the collective bargaining agreement (App. A P.C., A 3; App. E P.C., A 38-42). By executing the NMFA, Transport admittedly agreed to ratify all acts taken or to be taken by the Trustees of the Central States Funds within the scope of their authority (App. A. P.C., A 3-4; D-5, p. 3, para. 8).[6] Transport also admittedly executed a "Participation Agreement" (pertinent to the

[5] An employee is "covered" under the NMFA if he performs any work in a specified "job classification" or employer "operation" (Article 2, App. E P.C., A 38). Depending on the particular Supplement (Local Cartage, Over-the-Road, Iron and Steel and Special Commodities), job classifications include such categories as drivers, chauffeurs, driver-helpers, dockmen, warehousemen, power lift operators, etc. (Appellees' Brief, p. 2). Union membership is *not* a prerequisite for "coverage" as the Sixth Circuit found (App. B P.C., A 16). A "covered" employee does not become "eligible" for contributions unless he has been on the payroll as a "regular" employee (as opposed to an "extra" or "temporary") for 30 days or more.

[6] References to the district court record will be indicated by a "D" followed by the entry and, where appropriate, page numbers. Transport admitted that it was contractually obliged to permit the Trustees to conduct an audit. However, it contended that the Trustees exceeded the "scope of their authority" by requesting records for employees not concededly "covered" by the NMFA. The district court rejected this argument. The Sixth Circuit agreed with Transport.

Pension Fund) and a Joint Application (pertinent to the Health and Welfare Fund) wherein the company reaffirmed its commitments (*see* App. A P.C., A 4).

Article III, Section 5 (sentence two) of the Trust Agreements provides: "The Trustees may by their representatives examine the pertinent records[7] of each Employer at the Employer's place of business whenever such examination is deemed necessary or advisable by the Trustees in connection with the proper administration of the Trust" (App. A P.C., A 5-6; App. F P.C., A 46). Pursuant to this provision, Central States sent Transport an "audit engagement letter" on December 5, 1979 (App. B; *see also* App. A P.C., A 6-7). This was the first time the Trustees of Central States attempted to examine Transport's records (Appellees' Brief, p. 9; D-8, p. 5), and they had *no particular cause* to believe Respondents were in violation of ERISA or their collective bargaining agreements. In other words, Transport had been selected for a routine random field audit covering the period 1977-1979.

The audit began on February 4, 1980. All requests for information, records and documentation had to be addressed to one Mr. Robert Sigler, "Director of Payroll of each Defendant company" (App. H P.C., A 85, 89). Notwithstanding the fact that Transport consisted of 16 *trucking* companies under contract with the *Teamsters*, Mr. Sigler asserted, *without any substantiation*, that 60% of the Respondents' "employees" were not "covered" by the NMFA, had not "consented to" the production of their records, and were not subject to the Trustees' audit. The Sixth Circuit accepted Mr. Sigler's allegation on its face, as if it had been an established fact (App. B P.C., A 16). In reality, one of the *express purposes* of the audit requested would have been to *verify* this allegation. However, Mr. Sigler unilaterally refused to authorize the production of *any* of these records on the *unverified and untested conten-*

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[7] "Pertinent records" for audit purposes include complete payroll registers or payroll summaries (covering *all* employees), IRS 941 FICA quarterly earnings reports, IRS W-2, W-3, W-4, and 1099 forms for all employees, check registers, drivers' logs, trip manifests, contracts with independent contractors, leases with all owner-operators, bills of lading, detention records, employees' time cards, and personnel files (with such sensitive items as medical records or personal family data deleted). Central Transport has stipulated to the entry of an injunction requiring it to preserve these (and other specified) records pending the outcome of the appeal and the eventual completion of the audit (D-38, 44).

tion that such persons, not being "covered" by the NMFA, could *never* be eligible for benefits from Central States and that the records were confidential (Sigler Aff., App. H P.C., A 94). The district court rejected this position (App. A P.C., A 10-12); the court of appeals reversed.

Transport not only refused access to payroll records and other pertinent data for this group of employees; Transport also denied access to any documents relevant to *concededly covered employees* if such document *also* contained information concerning *allegedly noncovered* employees. It thus refused to produce (except for one three-month period in 1977) IRS 941 quarterly earnings forms, although tax forms are a reliable source for the independent verification of employee earnings (Sigler Aff., App. H P.C., A 93-94). Transport did little more than produce documents already in Central States' possession as well as an "insurance exception listing." (This is a document generated by the employer listing those individuals and time periods for which Transport *concedes* its legal obligation to the Funds. *See* Pasia Aff., App. H P.C., A 85-87. The employees on this list are those *ineligible* for the company's own pension plan *as determined by the company*. Absent a clerical error, this list would "match" any payroll ledgers for *concededly covered employees*.)

The auditors were requested to leave the premises on March 28, 1980 although the audit was incomplete both as to the records produced and companies audited (*see* O'Sullivan and Pasia Aff's., App. H P.C., A 83, 88).

On the basis of an incomplete examination of the records only of *concededly covered employees*, the auditors determined that Transport engaged in four kinds of underreporting, resulting in the following alleged delinquencies: at least $172,303.50 to the Pension Fund and at least $96,059.00 to the Health and Welfare Fund (O'Sullivan Aff., App. H P.C., A 83-84).[8] The court of appeals referred to

[8] "Late activation" (failure to report newly hired employees after the 30-day waiting period); "early termination" (reporting premature termination dates with concomitant failure to remit contributions for weeks worked); failure to remit required contributions for certain employees on sick leave; failure to remit contributions for certain employees who worked part of a week during which there was a strike. Audit findings represent only potential liability. These figures are subject

(Footnote 8 continued on Page 9)

these sums as *mere* "instances of underreporting" (App. B P.C., A 17, 30) and did not regard a general audit as justified, reasonable or prudent in view of these results.

The auditors also discovered that four employees on whose behalf Transport *was* remitting contributions were not listed on the payroll pertaining to covered employees. Instead, they were listed on the office payroll (Pasia Aff., App. H P.C., A 87). There was no explanation why these employees were entitled to contributions when the NMFA did not "cover" office personnel. Transport also refused to produce the office payroll register so that Central States could discover whether any other reporting discrepancies existed. Because the coverage status of these employees was unclear, the court of appeals expanded the scope of the audit to include the records of *these four employees*, but nevertheless asserted that general audits were arbitrary and capricious notwithstanding the fact that this kind of reporting discrepancy *illustrated* just how covered employees could be placed on an office payroll and shielded from the eyes of the auditors in accordance with Respondents' theory of confidentiality.

It is important for this Court to be completely clear that Central States' audit of Transport was not "triggered" by any of the above findings, as the court of appeals erroneously concluded (App. B P.C., A 17, 30); these findings were the *result* of a random *limited* audit. Moreover, in order for the above events to be meaningful, some indication of the statutory context is necessary as are some facts concerning the internal operation of the Central States Funds and the function of audits, which facts were presented to the courts below.

3. Statutory context

In 1974, Congress enacted ERISA in an attempt to prevent the great personal tragedies that had occurred in the past when employees reached retirement age only to discover that the benefits they had worked for and expected

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(Footnote 8 continued from Page 8)

to a consensual process of conciliation between the Funds and Transport or to further judicial proceedings in which Central States, as Plaintiff, will have the burden of proving Transport's liability. Audits can also result in a credit to the employer's account, possibly even to a return of contributions mistakenly made. 29 U.S.C. § 1103(c)(2)(A)(ii).

were not available due to careless trust administration and improper funding and vesting practices.[9] Among the goals to be promoted by the new Act were: the establishment of "standards of conduct, responsibility and obligation for the fiduciaries of employee benefit plans; adequate disclosure to participants; and adherence to minimum funding and vesting standards (29 U.S.C. § 1001).

Under ERISA, the trustees of such plans were given "exclusive authority and discretion to manage and control the assets of the plan" (29 U.S.C. § 1103), and "trustee responsibilities" were generally conceived to be "nondelegable" (29 U.S.C. § 1105). While the details of trust administration were to be set forth in mandatory written trust instruments (29 U.S.C. § 1102), the trustees were subject to an overriding statutory obligation to act "with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent man acting in like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims" (29 U.S.C. § 1104(a)(1)(B)).

ERISA requires pension plans to award credit to "participants" on the basis of "hours of service". A "year of service" leading toward the vesting of benefits is a calendar year, a plan year, or any consecutive 12-month period designated by the benefit plan in which a participant has completed *1,000 hours of service* (29 U.S.C. § 1052(a)(3)(A) and (C) and 29 U.S.C. § 1053(b)(2)(A)). These computations *must* include any hour for which an employee is directly or indirectly paid, or *entitled to payment* by an employer participating in a pension plan (29 C.F.R. § 2530.220b-2(a)(1) and (2)). Indeed, Advisory Opinion 76-89 issued by the DOL expressly states that credit must be given "*solely on the basis of service performed for a participating employer, regardless of whether that employer . . . has made or defaulted on his required contributions*" (31 August 1976, BNA *Pension Reporter*, No. 221, Jan. 8, 1979, emphasis added; *see* App. G P.C., A 70-74).[10]

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[9] *See Nachman Corp.* v. *PBGC*, 446 U.S. 359, 374-375 (1980); *PBGC* v. *R.A. Gray & Co. (No. 83-245)*, 52 U.S.L.W. 4810 (June 18, 1984).

[10] The Sixth Circuit acknowledged that benefits are not contingent on employer contributions in *Van Gunten* v. *Central States, Southeast and Southwest Areas Pension Fund*, 672 F.2d 586 (6th Cir. 1983).

Regulations promulgated pursuant to ERISA permit pension plans to employ "functional equivalents" to the "1,000 hour rule" noted above. 29 C.F.R. § 2530.200b-3(a) and (e). Central States has employed a "functional equivalent" based on full weekly contributions since its establishment in 1955 (D-8, p. 3). Twenty weeks of contributions entitle a participant to one year of *vesting* credit and one-half year of credit toward a twenty-year retirement benefit. An employer must remit a full weekly contribution if a participant has worked any part of the week. By the same token, the participant must be given a full week of credited and funded service by Central States regardless of the absence of employer contributions (D-8, p. 3). This funding practice makes the accuracy of employer reporting all the more important. Conversely, omissions cause a greater potential drain on fund assets and hence require greater Trustee vigilance directed toward their prevention.

Significantly, Section 209 of ERISA (29 U.S.C. § 1059) requires *employers* to "maintain records with respect to each of his *employees* sufficient to determine the benefits due *or which may become due to such employees*" (emphasis added). Unlike records supporting documents required by *plans* to be filed with the DOL and the IRS (29 U.S.C. § 1027), there is no six-year guideline for the retention of *employee* records by *employers*, since vesting and eligibility questions often involve much longer time frames.[11]

Finally, ERISA requires trustees to provide participants with Summary Plan Descriptions. In addition, benefit status reports must be provided at least once a year if requested. 29 U.S.C. §§ 1021, 1022, 1024, 1025; App. G P.C., A 56-66.

Pursuing the goals set forth in ERISA and carrying out the tasks imposed upon them, the Central States Trustees determined on the basis of years of experience in trust administration that random general audits of participating

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[11] Sections 3(6) and 3(7) of ERISA (29 U.S.C. § 1002(6), (7)) define, respectively, the terms "employee" and "participant." "The term 'employee' means any individual employed by an employer." "The term 'participant' means any employee or former employee of an employer . . . *who is or may become eligible* to receive a benefit of any type *from an employee benefit plan which cove s employees of such employer* . . ." (emphasis added).

employers' tax and payroll records[12] are the single most reliable and effective means of uncovering delinquent contributions and identifying employees potentially eligible for service credits, plan benefits and disclosure. Audits, of course, also reveal the presence of *ineligible* persons for whom contributions should not have been made or accepted. For actuarial reasons, it is important for the Funds to discover this class of individuals too. Significantly, the DOL and the IRS have approved field audit programs (Reg. 76-1, 41 F.R. 12740; March 26, 1976).

4. Central States' audits and their function

An employer's obligation to contribute to Central States is established in the collective bargaining agreement, which the Trustees have no role in negotiating. The employer and the union determine which job classifications will be covered. The Funds prepare a schedule of benefits which specified contribution rates can provide. The employer and the union select the benefits and rates they can afford. Upon contractually agreeing to participate in the trusts, the employer submits a list of employees "covered" by the collective bargaining agreement and "eligible" for contributions, *supra*, fn. 5. Initially verified by the local unions, this list constitutes the "base group." Thereafter, Central States must rely on the employer to accurately report fluctuations in the base group, for example, by adding newly hired "covered" employees as well as by reporting terminations (App. A P.C., A 6).[13]

[12] As used herein, a "random" audit means one in which an employer is selected without any reason to believe it is not reporting correctly. The employer does receive prior notice of the audit through an "engagement letter" from the Funds. The term "general" audit means that the Funds request access to pertinent records relating to the employer's complete work force, subject to safeguards to protect confidentiality. *Infra*, pp. 14, 15, 16, 31, 45.

[13] *See U.S.* v. *S & Vee Cartage*, 704 F.2d 914 (6th Cir. 1983). Here, the Sixth Circuit acknowledged that "Employee Billing Changes and Corrections" forms and "Monthly Contribution Reports" submitted by employers, respectively, to the Central States Pension and Health and Welfare Funds, "constitute the primary source, if not the sole source, available to trustees of pension and welfare funds with respect to the names of the employees covered and the amount of contributions made by employers." Defendants were convicted under 18 U.S.C. § 1027 for making false statements on these reports. Some of the reporting discrepancies were uncovered by a prior Central States audit.

Because of the size of the Funds and the geographical distribution of their constituency, contributions are remitted pursuant to a system of self-reporting, i.e., an honor system. Approximately 12,000 employers with employees in 40 states contribute to the two Funds pursuant to thousands of different collective bargaining agreements executed between themselves and Teamster Locals (App. B P.C., A 30). Since the Central States Funds are based in Chicago, Illinois, there is no way for the Funds to physically monitor employer reporting absent a field audit program, and to verify that the reported amounts are correct.

While many employers report correctly, substantial discrepancies do occur, typically, underreporting and nonreporting. An employer who "underreports" fails to contribute appropriately on behalf of employees he *concedes* are covered by the collective bargaining agreement and whom he has at some time reported to the Funds, whether by including them in the base group or by subsequently adding their names on monthly reporting forms. An audit of the records of concededly covered employees can detect this kind of misreporting. Such an audit of Transport revealed underreporting in the alleged amount of $268,362.50.

An employer who engages in the practice of "nonreporting" simply omits covered employees from the base group and never subsequently reports them to the Funds, thus eroding the actuarial solvency of both Funds and potentially increasing the unfunded vested benefits liability of the Pension Fund.[14] Audits of the records only of concededly covered employees (as mandated by the court of appeals) clearly cannot detect or remedy nonreporting.

Numbers best illustrate the magnitude of the problem of nonreporting. If only 10% of the 12,000 employers in the pool omit only one single employee from their contribution reports, the annual loss of income to the Pension Fund would be approximately $3,120,000.00 ($50.00 per week per employee × 52 weeks × 1,200 employers) (Petition for Rehearing *en banc*, p. 10).[15] Multiply even a fraction of this

[14] *See* Petition for Certiorari, p. 8, fn. 7 for a discussion of the impact of misreporting on a plan's underfunding.

[15] This formula assumes a weekly contribution rate of $50.00. Many employers, including Respondents, contribute pursuant to the NMFA. The current contribution rate under this contract is $55.00. *See* Brief of Amicus Arthur Young in Support of Petition, p. iv, v, 17.

figure by 2,000 pension funds in the United States and the potential net loss is staggering.

Fund audits are designed to intrude as little as possible on privacy rights, and "pertinent records" relating to allegedly "noncovered" employees are limited in the typical situation. However, as a general rule, access to complete payroll registers and IRS 941 forms is a minimum requirement for an independent audit. Indeed, the auditor's first objective is to assure himself that he is looking at an employer's "complete" employee population. If separate payrolls are kept, the auditor generally totals up the individual records and compares these totals with the gross payroll figure listed on the 941 tax form prepared quarterly for FICA purposes to document the employer's withholding tax liability. At this stage of the audit, *the dollar totals* are most important. Therefore, the auditor may, to accommodate confidentiality interests, permit the employer to delete the dollar figures entered for named individual corporate officers, providing that the employer adequately documents the identity of these individuals as officers. If a discrepancy exists between payroll totals and the 941 figure, further investigation is necessary. For, unless a clerical error can be shown, the suspicion naturally arises that additional payrolls exist and that people listed on an omitted or "ghost payroll" may be doing bargaining unit work. There is also the possibility that cash disbursements have been made.[16]

IRS 1099 forms (nonwage income) must also be investigated. An unusual amount of income reported on a single

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[16] *See* Petitioners' Supplemental Brief, p. 3 and Appendix (N.Y. Times, July 6, 1983: cash disbursements allegedly responsible for defrauding certain employee benefit trust funds of more than ten million dollars). An inquiry made subsequent to the filing of that Brief revealed that one of the construction companies under investigation, Prince Carpentry Inc., and its principals pled guilty to a six-count information charging conspiracy to defraud, mail fraud, and filing false corporate tax returns and agreed to pay the affected employee benefit funds $320,000.00 in back contributions on behalf of those covered employees who had been paid "off the books" in cash. *U.S.* v. *Prince Carpentry, Inc., et al.*, 84-188 (E.D.N.Y., March 20, 1984). The defendants' scheme, as shown by the information and a transcript of the guilty pleas, was that the company failed to report all employee work history and paid cash salaries to employees who were willing to work for a lower, but unreported wage. The case is significant not only with respect to the magnitude of the *employer's nonreporting;* it also shows how *employees* could be induced *not to report a company's fraud to the benefit funds* affected either out of ill-conceived self-interest or legitimate fear.

1099 form or the presence of a significant number of 1099 forms may raise a question of coverage, depending on the name which appears on the form and the type of company being audited.[17] For example, lessors of trucks receive 1099 forms reflecting rental income. If a lessor also drives his truck and is a bona fide independent contractor, the 1099 form will also reflect his earnings as a driver. However, lessor-drivers or "owner-operators," as they are known in the industry, may be "employees" and hence "covered" by the collective bargaining agreement depending on the regularity of employment and the degree of control of the carrier. Moreover, under the NMFA, while subcontracting is permissible under specified conditions, subcontracting on a regular basis may trigger contract wages and other terms and conditions of employment, including pension and health and welfare benefits. Access to complete records is particularly critical in this area.

If the payroll and 941 totals match, and there are no problems with the 1099 forms, the auditor spot-checks personnel files of allegedly noncovered employees. If it appears that employees listed on the payroll for noncovered employees do not in fact perform bargaining unit work, that is the end of the audit as far as this group is concerned. Even with regard to the covered employees, the audit is limited to essential records: if two documents verify the accuracy of reporting, four will not be demanded.

Substantial safeguards are also offered to protect confidentiality.[18] However, in accordance with generally accepted auditing standards which require at least some independent verification,[19] the audit cannot be limited solely to *employer-selected* records of one segment of its work force, for example, the records of those employees the employer *concedes* are covered by the collective bargaining agreement. If limited only to these records, the Trustees might

[17] Clearly, if the name of an attorney or a plumbing company appears on a 1099 form contained in the records of a trucking company signatory to the NMFA, the auditor can reasonably assume that no such coverage issue will be involved.

[18] The safeguards enunciated in *Central States, Southeast and Southwest Areas Pension Fund* v. *Theut Products*, No. 82-71080 (E.D. Mich. 1982), are standard (App. I P.C., A 96-99).

[19] *See*, for example, SEC Accounting Release No. AS-19; CCH Fed. Sec. Laws Repts. § 72,020 and *infra*, fn. 41, p. 41.

never discover the existence of covered employees the employer did not report in the first place, or they might discover them only at some later time when the employer was already out of business or bankrupt or after the statute of limitations had run, thus precluding a recoupment action as suggested by the court of appeals (App. B P.C., A 34).

5. Proceedings below

Carefully analyzing the language of various provisions of the Trust Agreements which afford the Trustees both specific powers and broad managerial discretion, the district court found that the Trustees had a contractual right to audit records relating to the employer's entire work force, and that this right would be enforced unless Transport could show an overriding interest in confidentiality (App. A P.C., A 10). In light of the safeguards offered by Central States and the relevance of the records for the purposes requested, the court found that on balance the Trustees' need for information outweighed the employer's interest in confidentiality (*id.*, A 11-12). The court then determined that ERISA supported the Trustees' request for records and that the audit demanded was neither arbitrary nor capricious (*id.*, A 12-13). Transport was ordered to produce the records requested, and the court refused to certify its order for an interlocutory appeal pursuant to 28 U.S.C. § 1292(b). Although the district court's opinion was rendered in the context of cross-motions for summary judgment, both parties having agreed that there was no genuine issue as to any material fact, Transport filed an appeal under 28 U.S.C. § 1292(a)(1).

The court of appeals took jurisdiction and reversed, finding neither a statutory nor a contractual basis for random general audits. While the court acknowledged that "the trustees must ensure that contributions to the Funds correlate with the disbursement of benefits from them" (App. B P.C., A 29), and that "entitlement to Funds' benefits . . . may also be established by the judicial or arbitral process where there is no concession that an employee, or one claiming under him or her, is a covered employee," it nevertheless restricted audits to the records of concededly covered employees and to the records of *particular individuals* as to whom the Trustees had established *reasonable cause* to believe they were covered re-

gardless of how they were classified by the employer or the Union. The court did not explain how such "reasonable cause" could be established absent antecedent production of records relating to a complete "employee universe" as this term is understood by accountants.

Completely misapprehending the purpose of the audit, as noted above, the court reasoned that on the basis of apparent "instances of underreporting for covered employees" (more than a quarter of a million dollars!) and "the receipt of monies for four employees whose coverage was not disclosed by the Union seniority list, Transport, or the Union," it would be "arbitrary and capricious" to audit "the records of all of Transport's employees" (*id.*, A 30); indeed, the court stated that no "prudent man" would authorize such an audit, if only because of the "expenses" involved (*id.*). In so concluding, the court appeared to elevate the cost factor above all other components of a "prudent" trustee decision (29 U.S.C. § 1104) and did so *without any evidence of the cost of this particular audit or of audits in general.*[20]

The court accepted as a fact that the majority of Transport's employees were not covered by labor agreements. However, there is *no* evidence in the record that this "fact" had been established or agreed to by Petitioners (*id.*, A 30). Nevertheless, the court objected to the Funds' audit on confidentiality grounds without addressing the relevance of the records for the purpose requested or the safeguards offered to protect privacy interests (*id.*, A 30). In contrast to the district court, the Sixth Circuit also rejected Central States' analogy to NLRB disclosure standards.

The court also noted, without citing *any* authority, that the Funds would be adequately protected through the efforts of the Union and the Secretary of Labor or of employees themselves.

Finally, the court limited the scope of the audit by narrowly construing the "Production of Records" provision of the Trust Agreements, substituting its own "wisdom" for

[20] There is absolutely no evidence in the record as to the cost of the audit either to Central Transport or, more importantly, to the Funds. This is very significant since the panel found that random general audits would be contrary to ERISA because of their *cost*; the suggestion is that such audits would be a waste of Fund assets and, for *this reason*, arbitrary and capricious. *Id.*, A 30.

the "discretion" of the Trustees, although the Trustees have plenary power to interpret the Trust Agreements and although their interpretation was both grammatically and logically reasonable as well as consistent with prior practice and good faith. Having narrowly interpreted this document so as to eliminate a *contractual* basis for the audit, the court was able to eliminate a *statutory* basis by stating that the nature and scope of the Trustees' fiduciary obligations under ERISA are limited by plan *documents* which in this case refer only to "covered employees." The court thus reached the clearly erroneous and circular result that absent *reasonable cause* to believe *particular* individuals were improperly omitted from coverage, the Trustees could *verify* the accuracy of *employer* reporting only by reviewing the records of employees the *employer conceded were covered*! This error was compounded by the clear suggestion that random audits that go beyond the records of concededly covered employees are *per se* arbitrary and capricious because they are too costly and too intrusive. Hence, even if a Trust Agreement spelled out in explicit detail the kind of audit requested by the Central States Trustees under the phrase "pertinent records," such a procedure would still be unenforceable as contrary to ERISA and public policy.

Central States therefore seeks a ruling not only that the Trust Agreements in their present form and as interpreted by the Trustees permit random general audits, but that *ERISA independently* permits trustees of employee benefit funds to request access to complete employee records, subject to safeguards to protect confidentiality, in order to verify the accuracy of reporting, to deter evasions, and to identify all eligible plan participants without the aid or intervention of third parties.

SUMMARY OF ARGUMENT

The issue in this case is whether trustees of multi-employer employee benefit funds may request access to complete employee records, subject to safeguards to protect confidentiality, when conducting random audits to verify the accuracy of reporting.

I.A. The trustees of Taft-Hartley funds have the right, under ERISA, to conduct surveillance audits and to request complete verification data in accordance with 29 U.S.C.

§ 1104(a)(1)(B), the "prudent man" rule. When Congress enacted ERISA in 1974 in order to protect the security and well-being of millions of American workers, it gave plenary powers to the trustees of employee benefit funds. Because the funds subject to the statute differed so greatly, Congress refrained from setting forth a detailed list of specific trustee powers. Instead, the legislature drafted a few affirmative duties and a few express prohibitions and generally contemplated that Trustees would act in accordance with common law principles of trust which would offer great flexibility and yet provide such established curbs on trustee action as good faith, reasonableness, and consistency. At the heart of the statute is merely a general mandate: trustees must act *solely* in the interests of participants and beneficiaries *and* with that degree of care, skill, diligence and prudence that is appropriate in the circumstances.

Under ERISA and corresponding regulations, trustees nevertheless have an *express* duty to collect contributions from employers, grant vesting credit and pension benefits to all eligible employees regardless of whether or not their employers have made corresponding contributions, and to provide Summary Plan Descriptions and benefit status reports to plan participants and beneficiaries. Under ERISA, as under the common law of trusts, trustees have *implied* powers to achieve *express* objectives. Audits are the *ordinary and natural means* for ascertaining and collecting contributions; for preventing a drain on fund assets by correlating disbursements from and contributions to the funds, and for identifying all eligible participants to whom a duty of disclosure is owed. *Random* audits enable the Trustees to implement the above objectives more effectively.

Access to *complete* records is dictated by the fact that meaningful audits require independent inquiry and independent verification of data. Central States, like the federal tax system, operates on a self-reporting basis. In policing this system, the Trustees cannot reasonably rely on the representations of the employer that employees who are *concededly covered* are the *only* employees who do, *in fact*, perform bargaining unit work and are therefore eligible for contributions.

Case law indicates that those charged with enforcing the Internal Revenue Code and the Fair Labor Standards Act are not required to accept the representations of the subject of the inquiry. *U.S.* v *Bisceglia*, 420 U.S. 141 (1974); *Fleming* v. *Montgomery Ward Co.*, 114 F.2d 384 (7th Cir. 1940). Nor are they subject to a cause standard. *U.S.* v *Powell*, 379 U.S. 48 (1964); *Oklahoma Press Publishing Co.* v *Walling*, 327 U.S. 186 (1946). Employee benefit funds, though private, are sufficiently affected with national public interest to permit their trustees, as federal fiduciaries, to enjoy similar investigative latitude commensurate with the nature of their task so long as they can provide safeguards to protect confidentiality.

In the area of employee benefits, post-ERISA case law suggests that the Sixth Circuit's limited audit/reasonable cause standard is unworkable and would not reveal misreporting 1) under prehire contracts, *McNeff* v. *Todd*, 103 S. Ct. 1753 (1983); 2) where an employer contests coverage under a collective bargaining agreement, *Bugher* v. *Consolidated X-Ray Service Corp.*, 705 F.2d 1426 (5th Cir. 1983); *Laborers* v. *Kaufman & Broad*, 707 F.2d 412 (9th Cir. 1983); 3) where an employer claims that an individual is an independent contractor, *Trust Fund* v *Hawg N. Action*, 651 F.2d 1384 (10th Cir. 1981); 4) where a collective bargaining agreement provides for contributions *measured by hours* of covered work performed by employees of a nonsignatory employer, *Walsh* v. *Schlecht*, 429 U.S. 401 (1977); and 5) where the collective bargaining agreement has been orally modified by the employer and union, *Waggoner* v. *Dallaire*, 649 F.2d 1362 (9th Cir. 1981). In such situations, employers, like Transport, would simply withhold the records of anyone not *concededly* covered. Thus, absent consensual access to complete records, trustees will have no alternative but to compel records through discovery, although increased litigation will have an adverse impact on the courts, on funds, and on the employers themselves. And, should courts not grant access to pertinent records through discovery, the Sixth Circuit will have created a privilege not countenanced by the Federal Rules of Evidence. Those who will ultimately suffer will be honest employers as well as participants and beneficiaries on whose shoulders funding gaps will fall.

I.B. This Court has made it unambiguously clear that Congress intended employee benefit trust funds to be independent from unions, that trustees are neutral fiduciaries and not part of the collective bargaining process, and that trustee powers set forth in properly executed trust agreements should not be lightly eroded. *NLRB* v. *Amax Coal Co.*, 453 U.S. 322 (1981); *Schneider Moving & Storage, et al.* v. *Robbins, et al.*, 104 S. Ct. 1844 (1984). Under ERISA, trustees have a *nondelegable* fiduciary duty to conduct audits and collect contributions. 29 U.S.C. § 1105; *Rosen* v. *Hotel and Restaurant Employees, Local 274*, 637 F.2d 592 (3d Cir. 1981); *Nichols* v. *Trustees of Asbestos Workers Pension Plan*, 3 EBC 1726 (D.D.C. 1982). The Sixth Circuit, in limiting the scope of Central States' requested audit of Transport, stated that the Funds would be adequately protected by the efforts of unions, employees themselves, and the Secretary of Labor. There is no authority to support this proposition, which is also in evident conflict with the spirit of the LMRA, ERISA, and the rationales of leading cases of this and other courts. It would be *quintessentially imprudent* for trustees to rely on third persons to monitor their self-reporting system since the persons recommended by the court of appeals 1) may have competing interests; 2) may lack sufficient knowledge to perform the task; and 3) may lack the physical or financial capability to do so. It would be *fundamentally unfair* to place the burden on employees since it is *employees* ERISA was enacted to protect in the first place!

I.C. ERISA requires employee benefit plans to submit annual financial reports which must be audited by an independent CPA in accordance with generally accepted auditing standards. A primary objective of the financial statement and the audit is to assure that the materials fairly present the ability of the plan to pay benefits when due. If a plan has an internal field audit program which itself operates in accordance with accepted procedures, this gives rise to an assumption that employers are generally complying with their contribution obligations and are reporting participants correctly. In such a case, the field audit program functions as an "internal accounting control" serving to authenticate the accuracy of the financial statements. Central States' independent auditor has approved of and relies

upon the Funds' internal field audit program. It has publicly stated that it could *not* rely on audits conducted in accordance with the Sixth Circuit's scope limitation. The Trustees would be *imprudent* if they failed to conduct audits in accordance with generally accepted standards which external accountants also utilize and upon which they rely.

II. The Sixth Circuit imposed a cause standard and therefore a scope limitation on Fund audits in accordance with its notions of confidentiality. In so doing, it rejected disclosure principles which have evolved under the NLRA in order to permit unions to perform their representational duties effectively. The key to disclosure under the NLRA is relevance. The Trustees have shown that the purpose of their inquiry is legitimate, that the manner of their inquiry comports with generally accepted auditing standards, that the materials requested are not only relevant to the inquiry but not reasonably accessible except from the employer, that safeguards exist to protect confidentiality, and that breaches of confidentiality are remediable. The Trustees' field audit program is a prudent method of enforcing ERISA. Unless the Trustees are granted access to an employer's complete employee records, no one will be able to conduct adequate surveillance audits and irreparable harm will be done to the Funds and their participants. Since, on balance, it is clear that the Trustees' need for information outweighs the employer's interest in confidentiality, the liberal discovery-type standard applicable under the NLRA should be equally applicable to ERISA. It is only in this way that the Trustees' will be able to perform their fiduciary duties effectively.

III. The Trustees have a *contractual* right to conduct the audit requested. Article III, Section 5, sentence 2 of the Trust Agreements governing the Funds *expressly* authorizes the Trustees to conduct on-site audits of an employer's "pertinent records." The Trust Agreements also authorize the Trustees to construe the provisions of these instruments and, as this Court recognized in its *Schneider* opinion, *supra*, all such constructions made in good faith are binding. The Trustees have always construed the term "pertinent records" to mean the tax, payroll, and related data necessary to conduct a professionally acceptable audit. This requires access to records concerning the *entire employee*

population. The Sixth Circuit translated the phrase "pertinent records" into the phrase "employee records" and then further limited the word "employee" so as to mean "concededly covered employee." The court of appeals substituted its own interpretation for that of the Trustees and hence departed from the proper standard of judicial review. Transport *contractually* agreed to comply with the terms of the Trust Agreements, including the Trustees' constructions thereof; the Trustees' interpretation was reasonable, logical, consistent, and made in good faith. In conducting random general audits, the Trustees seek only to *establish for themselves* that all employees performing bargaining unit work are receiving appropriate contributions. The Sixth Circuit's construction of the Trust Agreements and the audit function is clearly erroneous.

ARGUMENT

I. ERISA PERMITS TRUSTEES OF MULTIEMPLOYER PLANS TO CONDUCT RANDOM GENERAL AUDITS TO VERIFY THE ACCURACY OF REPORTING AND TO IDENTIFY ALL ELIGIBLE PLAN PARTICIPANTS

I.A. Random general audits are "prudent" within the meaning of 29 U.S.C. § 1104

I.A.1. Trustees have express and implied powers under ERISA as under the common law; the right to audit is an implied power

Audits and accountings are routine trustee activities.[21] Nevertheless, they are *specific* to particular purposes and situations and hence unsuitable for explicit, detailed, and generally applicable statutory formulation. Thus, it is not surprising that the court of appeals failed to find an express provision in ERISA authorizing and setting forth a procedure for the conduct of "complete" audits. Having recognized that employee benefit funds differ from each other in

[21] Bogert, *The Law of Trusts and Trustees*, Chap. 46, *Accounting and Compensation* (rev. 2d ed. 1980). In the context of employee benefit trusts, the trustees' right to audit contributing employers' records was rarely challenged prior to 1980. (*see* Appellees' Brief, pp. 22-26, and cases cited therein.) Transport itself conceded that there was a *single* case on point: *Central States, et al.* v. *CRST*, 641 F.2d 616 (8th Cir. 1981). *CRST* was substantially overruled in *Robbins* v. *Prosser*, 700 F.2d 433 (8th Cir. 1983), aff'd, 104 S. Ct. 1844 (1984).

many respects, the drafters of ERISA refrained from setting forth a comprehensive list of specific acts which trustees were required to perform in order to fulfill their statutory fiduciary obligations and effectively administer the assets committed to their care. Instead, ERISA contains a few affirmative duties[22] and a few specific prohibitions (29 U.S.C. § 1106), and leaves the details of trust administration to be articulated in mandatory written trust agreements, specific to each fund.

Nevertheless, 29 U.S.C. § 1104 is a core provision of ERISA and sets forth the fiduciary obligation and prudent man rules of the statute, which provide the measure by which Trustee activities must be gauged where an act is neither expressly commanded nor expressly prohibited.

In formulating this overriding provision, however, Congress purposefully painted with a broad brush. This is because ERISA was intended to codify "principles applicable to the law of trusts." 3 *U.S. Code Cong. & Ad. News* 5186 (1974); *NLRB* v. *Amax Coal Co.*, 453 U.S. 322 (1981); *Robbins, et al.* v. *Prosser's Moving & Storage Co. and Schneider Moving & Storage Co.*, 700 F.2d 433, 439 (8th Cir. *en banc*, 1983), *aff'd*, 104 S. Ct. 1844 (1984). As Congress recognized, trust principles permit a maximum of flexibility and discretion while affording such well-established curbs on trustee conduct as good faith, reasonableness, and consistency.[23]

Under the common law of trusts, trustee powers are of two classes: express and implied. *Express* powers are those which are granted and set forth in trust instruments or statutes; *implied* powers are those which are inferred therefrom because they are necessary or appropriate for carrying out the *express* purposes of the trust. Section 3(a) of the 1964 Uniform Trustees' Powers Act provides:

From time of creation of the trust until final distribution of the assets of the trust, a trustee has the power to

[22] For example, the duty to file annual reports (29 U.S.C. §§ 1023, 1024); to furnish participants with Summary Plan Descriptions (29 U.S.C. §§ 1022, 1024, 1025); to diversify investments (29 U.S.C. § 1104(a)(1)(C)); the duty to retain records (29 U.S.C. §§ 1027, 1059).

[23] While ERISA imposed more stringent fiduciary standards on trustees of employee benefit plans, case law antedating passage of the statute had long since indicated that pension and welfare plans were to be regarded as common law trusts and their trustees as fiduciaries. *See Kosty* v. *Lewis*, 319 F.2d 744 (D.C. Cir. 1963).

> perform without court authorization, every act which a prudent man would perform for the purposes of the trust including but not limited to the powers specified in subsection c [express powers].[24]

This has been construed to mean that a trustee has certain "inherent" powers which are implied from his office. *See* Bogert, *The Law of Trusts and Trustees* § 551. Put differently, an "implied" power is one which can be regarded as the *ordinary and natural means for obtaining an express and intended result* (*id.*, p. 41).

The authority to audit employer records may be implied or inferred from several express provisions of ERISA and/or corresponding regulations. In the first place, 29 U.S.C. § 1103 grants trustees "exclusive authority and discretion to manage and control fund assets". To this end, trustees have the unquestionable power, both express and implied, to *collect* delinquent contributions. Indeed, failure to do so through negligence or complicity would be a "breach of fiduciary duty" under 29 U.S.C. § 1104 and a "prohibited transaction" under 29 U.S.C. § 1106.[25] In enacting 29 U.S.C. § 1145 and 29 U.S.C. § 1132(g)(2), Congress *expressly* intended that *employers* adhere to their contribution obligations as set forth in collective bargaining agreements or multiemployer plans and that *trustees* enforce such contracts and plans, providing plans with stringent make-whole remedies for successful enforcement. An audit to encourage employer compliance, to verify the accu-

[24] Although the Uniform Trustees' Powers Act does not purport to cover employee benefit trusts (Section 1, Definitions), it contains a "prudent man" rule similar to, though less stringent than, that set forth in 29 U.S.C. § 1104. The Act is therefore relevant to the common law basis of ERISA.

[25] It is a "prohibited transaction" to extend credit to a "party in interest" or to allow fund assets to remain in the hands of such party for his use or benefit (29 U.S.C. § 1106(a)(1)(B) and (D). An employer, any of whose employees are covered by an employee benefit plan is a "party in interest" (29 U.S.C. § 1002(14)). Contributions owed under collective bargaining agreements but not paid are fund assets (*see* DOL Advisory Opinion, 78-28 (App. G P.C., A 73). DOL Reg. 76-1 (41 F.R. 12740) also makes clear that trustees may breach their fiduciary duties and commit a prohibited transaction if they fail to maintain orderly and systematic procedures for the determination and collection of employer contributions. Claims may be compromised only for prudent business reasons, taking into account the legal merit of the claim, the potential cost of collection relative to the amount in controversy, and the ability of the employer to pay if a judgment is rendered.

racy of reporting, and to determine whether any amounts are delinquent is the *ordinary and natural means* for implementing the express power to collect.

Pension plans are also *expressly* required to award vesting service credit and benefits to eligible participants based on hours worked in covered employment *regardless of employer contributions*. An audit is the *ordinary and natural means* for "correlating" disbursements from and contributions to pension funds, a duty which the Sixth Circuit perceived without approving the method selected by the Trustees to prevent a drain on fund assets and an increase in unfunded vested benefits liability.

The trustees of multiemployer plans are also *expressly* required to provide Summary Plan Descriptions to eligible plan participants (29 U.S.C. §§ 1022, 1024). Moreover, they must provide them with benefit status reports once a year upon request (29 U.S.C. § 1025). An audit is the *ordinary and natural means* for identifying eligible plan participants with a view toward informing them of their statutory rights. To the extent an employer engages in nonreporting (i.e., completely omits a covered employee from the "base group" and subsequent remittance forms), random general audits allow trustees to fulfill their disclosure obligations. There is no authority for the court of appeals' suggestion that an employee who *fails* to receive a Summary Plan Description or benefit status report should thereby be on notice to contact the Funds with regard to his or her coverage and eligibility and that failure to do so might create an estoppel in favor of the Funds. I *infra*, p. 39.

It is clear from the foregoing that benefit plan trustees have an *implied* statutory power to conduct an audit of some kind. The *permissible scope* of the audit, however, requires application of the "prudent man rule" (29 U.S.C. § 1104) taking into account such considerations as the purpose of the audit; the size of the fund; the type of industry or industries in which contributing employers are engaged; the type of jobs performed by participants (including such factors as transcience,[26] visibility, and potential overlap

[26] This is of particular importance in construction industries. *See* Amicus Brief of *Bricklayers, et al.*, pp. 4-5.

with noncovered work);[27] the nature of fund and/or employer recordkeeping; plan experience with regard to accurate reporting; and generally accepted auditing standards.

The type of audit at issue here is a "random audit."[28] Plan experience has generated the need for such periodic investigations: to deter evasions; to verify that all persons actually performing covered work are being reported; to enhance Trustee protection of the benefit status of every person entitled to coverage and disclosure under ERISA; to prevent reporting on behalf of ineligible individuals; to foster actuarial solvency; to prevent increases in unfunded vested benefits liability; to comply with standard auditing practices; and to assure that Trustees maintain an *independent* role in the administration of the trusts. The court of appeals was clearly erroneous in limiting the scope of the audit. Basic dictionary definitions of the word "audit" indicate that the Trustees' request for access to complete employee records, their healthy skepticism, and their refusal to rely exclusively on employer-selected and employer-generated documents was reasonable, logical, and practical — in a word, prudent.

I.A.2. Access to complete records is necessary for a genuine and independent audit given a self-reporting system: the IRS and FLSA analogies

Black's Law Dictionary defines an audit as follows: "Sometimes restricted to a mere mathematical calculation or process, but, in its generally accepted sense, includes an investigation and weighing of evidence and deciding of whether entries in books are true and correct." Webster's *New World Dictionary of the American Language* states that an audit is "a regular examination and checking of accounts or financial records." The *Oxford*

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[27] In the trucking industry, for example, a truck driver may be a "covered employee" or a noncovered "independent contractor owner-operator" depending upon the precise circumstances of his employment and the application of agency principles. Since "owner-operators" are typically dispatched from their homes and travel with full truck loads from shipper to receiver, their work is particularly invisible to the union.

[28] Most funds, including Central States, also conduct audits upon certain requests ("referral audits") as well as in conjunction with litigation to ascertain damages ("delinquency audits"). The same principles that apply to random audits apply *a fortiori* to cause-generated audits.

English Dictionary describes an audit as a "systematic examination of accounts, so as to ascertain their accuracy." An "auditor" is one who "verifies" the accounts of monies in the hands of others by reference to other documents. *Id.*

From the Funds' perspective, an audit is a fact-finding and verification procedure similar in purpose to that used by the IRS pursuant to 26 U.S.C. §§ 7601 and 7602 (App. C). Like the IRS, Central States cannot *rely solely* on the self-selected records of an employer who has been chosen for an audit. To state the obvious: "*An audit in order to be effective must be independent. The taxpayer* [and by analogy contributing employers] *cannot dictate what information is to be examined for mistake or evasion.*" *U.S.* v. *Davey*, 404 F. Supp. 1283, 1284 (S.D.N.Y. 1975, emphasis added).

In *U.S.* v. *Bisceglia*, 420 U.S. 141, 145-146 (1974), Chief Justice Burger described the audit function of the IRS in terms which are so pertinent to the issue at bar that Petitioners are unable to plead their request for access to complete employee records more eloquently than by quoting from the Court's Opinion in full:

> We begin examination of these sections [26 U.S.C. §§ 7601 and 7602] against the familiar background that our tax structure is based on a system of self-reporting. There is legal compulsion, to be sure, but basically the Government depends upon the good faith and integrity of each potential taxpayer to disclose honestly all information relevant to tax liability. Nonetheless, it would be naive to ignore the reality that some persons attempt to outwit the system, and tax evaders are not readily identifiable. Thus, § 7601 gives the Internal Revenue Service a broad mandate to investigate and audit "persons who *may be* liable" for taxes and § 7602 provides the power to "examine any books, papers, records, or other data which may be relevant . . . [and to summon] any person having possession . . . of books of account . . . relevant or material to such inquiry." Of necessity, the investigative authority so provided is not limited to situations in which there is probable cause, in the traditional sense, to believe that a violation of the tax laws exists. *United States* v. *Powell*, 379 U.S. 48 (1964). The purpose of the statutes is not to accuse, but to inquire. Although such investigations unquestionably

involve some invasion of privacy, they are essential to our self-reporting system, and the alternatives could well involve far less agreeable invasions of house, business, and records.

We recognize that the authority vested in tax collectors may be abused, as all power is subject to abuse. However, the solution is not to restrict that authority so as to undermine the efficacy of the federal tax system, which seeks to assure that taxpayers pay what Congress has mandated and to prevent dishonest persons from escaping taxation thus shifting heavier burdens to honest taxpayers.

Because of its size, Central States cannot operate other than through a system of self-reporting. Experience has shown that a significant number of employers do attempt to "outwit the system," that "evaders are not readily identifiable," and that the availability of criminal sanctions for misreporting (18 U.S.C. § 1027) does not have the deterrent effect that Transport would put forward as an alternative to complete Trustee audits.[29] To paraphrase *Bisceglia*, random general audits are "essential to [the] self-reporting system" of most multiemployer plans to "assure" that contributing employers "pay what Congress has mandated and to prevent dishonest persons from escaping their obligations," thereby "shifting the burden to honest" employers as well as to participants and beneficiaries who rely on the solvency of the pool.

In the employee benefits sphere, as in our tax system, a cause standard can only frustrate necessary investigative activity. Indeed, under *U.S.* v. *Powell*, 379 U.S. 48, 57-58 (1964), and its progeny, IRS audits (whether consensual or summoned) are considered justifiable if their purpose is legitimate, if the materials requested are relevant to the inquiry and not already in the possession of the government, and if administrative procedure is complied with. Petitioners submit that multiemployer employee benefit

[29] In early 1983, at the time the Sixth Circuit decided *Central Transport* and limited the scope of the audit, only *one* reported case existed in which an employer was convicted for falsifying reports to employee benefit funds. *U.S.* v. *S & Vee Cartage*, 704 F.2d 914 (6th Cir. 1983). Petitioners are not aware of a subsequent flurry of convictions for misreporting. (Only *one* has thus far resulted from the Drywall investigation, *supra*, p. 14, fn. 16). On the other hand, collection actions for delinquent contributions continue to be filed with regularity.

funds, while private, are affected with sufficient national public interest (29 U.S.C. § 1001(a)) to permit their trustees, as federal fiduciaries, to investigate employer records under *Powell*-type criteria, if the trustees act in accordance with systematic procedures[30] and protect confidentiality.

Significantly, in rejecting a "probable cause" standard for the enforcement of IRS summonses in *U.S.* v. *Powell*, *supra*, this Court drew an analogy to investigations pursued under the Fair Labor Standards Act, a statute whose remedial purposes and actual remedies closely parallel those of ERISA. Random general audits by benefit fund trustees are analogous, if not functionally equivalent, to the random inspection of records conducted by the Administrator of the Wage and Hour Division of the DOL pursuant to Section 11 of the FLSA. Courts construing the inspection powers of the Administrator have rejected most of the arguments raised by Transport and accepted by the Sixth Circuit. *See Fleming* v. *Montgomery Ward Co.*, 114 F. 2d 384 (7th Cir. 1940), *Cudahy Packing Co.* v. *Fleming*, 122 F. 1005 (8th Cir. 1941), and *Oklahoma Press Publishing Co.* v. *Walling*, 327 U.S. 186 (1946). These cases and their relevance to the issue at bar were discussed in the Petition, pp. 20-23. Two points deserve repetition. First, *in contrast to* the FLSA, Congress in enacting ERISA left the task of conducting routine audits primarily to fund trustees while assigning the DOL the responsibility for ensuring that the trustees perform their fiduciary duties (*infra*, p. 39-40). Second, trustees, *like the Administrator*, require access to complete employee records if they are to perform their duties "intelligently" and "prudently," that is, in possession of the "substance" rather than the "shadow" of authority. They are *not* required to take the word of the subject of the inquiry.

The fact that employers can be required to make available complete employee records to Fund auditors without a prior showing of reasonable cause does not leave them unprotected and remediless. The Central States Trust Agreements require that Trustee requests for information and

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[30] Central States' audits always commence with an "audit engagement letter" and are conducted in accordance with procedures set forth in a written audit manual. This manual has recently been enlarged and revised by a staff of In-House Certified Public Accountants who comprise the "Field Audit Group."

records be reasonable and specifically related to the necessary and proper administration of the funds. Names and addresses of participants and beneficiaries are *expressly* confidential (Article III, Section 5). Article III, Section 14(a) empowers the Trustees to enter into agreements necessary for carrying out the terms of the Trust Agreement. Article IV, Section 14(e) empowers the Trustees to do whatever acts are necessary to protect trust property whether or not expressly authorized in the trust instrument. The Trust Agreements clearly encompass the development and implementation of fund policy. The *Theut Products* protective order (App. I P.C.) reflects Fund policy on audit confidentiality. This policy is noted in the Funds' audit manual. The Trust Agreements are normally incorporated by reference into two instruments executed by the employer and the union: the collective bargaining agreement and the participation agreement. (Transport executed *three* such incorporating agreements, *supra*, pp. 6-7.) If the Trustees' audit is perceived as being "unreasonable" or unrelated to proper trust administration, or if confidentiality is intentionally breached, there is no authority to suggest that the employer would be precluded from filing suit in order to obtain, as appropriate, either an injunction or damages.

I.A.3. Post-ERISA case law illustrates why audits limited to the records only of concededly covered employees would endanger fund assets and hence be imprudent

On April 18, 1984, this Court unanimously affirmed the Eighth Circuit's *en banc* opinion in *Schneider Moving & Storage Co.* v. *Robbins, et. al., supra*, finding that the Trustees of the Central States Funds were not required to exhaust the arbitration mechanisms of the collective bargaining agreements at bar prior to seeking judicial enforcement of those provisions of the Trust Agreements authorizing audits and collections. Prosser had refused to permit an audit and requested arbitration concerning the Trustees' right to audit as well as a determination of the scope of the audit. Schneider had permitted an audit but requested an arbitration of whether certain employees were "covered" by the collective bargaining agreement and entitled to contributions. Justice Powell, writing for the Court, observed:

> These are multiemployer trust funds. Each of the participating unions and employers has an interest in the

> prompt collection of the proper contributions from each employer. *Any diminution of the fund caused by the arbitration* requirements of a particular employer's collective-bargaining agreement would *have an adverse effect on the other participants.* The enforcement mechanisms established in the trust agreements protect the *collective interests of the parties from the delinquence of individual employers* by allowing the trustees to seek prompt judicial enforcement of the contribution requirements. It is *unreasonable to infer* that these parties would agree to subordinate those mechanisms to whatever arbitration procedures might be required by a particular employer's collective-bargaining agreement. (Slip op. at 9, footnotes omitted, emphasis added)

It is even more unreasonable to *infer*, as did the Sixth Circuit, that these parties, not to mention the Trustees, would be willing to subordinate the determination and collection of contributions receivable to a particular employer's notions of the permissible scope of an audit or to that employer's concession regarding the contractual coverage of its employees and their actual or potential eligibility for fund benefits. In point of fact, unless pertinent records relating to a complete employee population are made available, *coverage disputes*, such as that involved in *Schneider* (and the conflicting Seventh Circuit case *Central States, Southeast and Southwest Areas Pension Fund, et al.* v. *Howard Martin*, 625 F.2d 171 (1980), are not likely to occur. Like Transport, the employer would simply withhold the records of those employees *it unilaterally determined were not covered*, thereby precluding the Trustees from discovering inaccuracies or omissions except by chance. The following reported decisions are representative examples of how employee benefit funds could easily be deprived of assets if the Sixth Circuit's "limited audit" theory were to prevail.

In *Jim McNeff* v. *Todd*, _____ U.S. _____, 103 S. Ct. 1753 (1983), an employer in the construction industry consistently refused to permit an audit and to remit contributions under a "prehire contract," claiming that its employees were not "covered" by a valid and enforceable collective bargaining agreement. An examination of records ultimately took place through the vehicle of pre-trial dis-

covery, and the funds collected some $5,000.00 upon this Court's finding that prehire contracts are enforceable without proof of union majority status unless and until they are overtly repudiated.[31] Had the *McNeff* audit been entirely consensual, and had the trustees been limited solely to the records of employees who the employer conceded were covered, the audit could not have taken place since the employer asserted that none of its employees were covered.

In *Laborers Health and Welfare Trust Fund, et al.* v. *Kaufman & Broad*, 707 F.2d 412 (9th Cir. 1983), a coverage dispute in a trustee collection action arose subsequent to a fund audit. The audit revealed and the trustees claimed $131,887.68 in unpaid pension contributions on behalf of a class of employees performing "callback work." The employer contended that "callback work" was not within the union's jurisdiction and that the employees performing it were not covered by the collective bargaining agreement. But for the audit, the trust fund in question would not have discovered that "the Company used nonunion labor for 'call-back work' and that no pension contributions were made for such labor." *See also Brick Masons Pension Trust* v. *F.K. Pullen*, 113 L.R.R.M. 3040 (C.D. Cal. 1983), in which a fund was awarded more than $44,000.00 in unpaid contributions revealed by an audit spanning a mere eight-month period.

In *Bugher* v. *Consolidated X-Ray Services Corp.*, 705 F.2d 1426 (5th Cir. 1983), a coverage dispute arose as the result of *two* audits, one conducted by the Central Pension Fund and one by the employer. The fund audit revealed alleged delinquencies of $104,312.33. The employer's rebuttal audit yielded a conceded delinquency of $143.00. The parties agreed that this gross discrepancy was due to the fact that the employer did not contribute for nonunion employees or for union employees performing cross-country pipeline jobs on the grounds that neither group was covered by the collective bargaining agreement. The district court held for the trustees and awarded the fund $101,039.93 plus

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[31] *See also Welfare Fund* v. *Overhead Door Co.*, 104 L.R.R.M. 2653 (D.D.C. 1980), reversed, 110 L.R.R.M. 2752 (D.C. Cir. 1982). Extremely concerned with delinquent contributions to employee benefit funds nationwide, Congress expressly repudiated the decision in the debates preceding passage of the Multiemployer Pension Plan Amendments Act of 1980, 126 Cong. Rec. (House) 23039 (Aug. 25, 1980).

audit expenses, attorney fees and interest. The court of appeals affirmed. Under the *Central Transport* ruling, the Funds would have been limited to the ludicrous amount of $143.00 for "concededly covered employees."

In *Audit Services, Inc.* v. *Rolfson*, 641 F.2d 757 (9th Cir. 1981), a payroll audit revealed that an employer had paid $40,000.00 in cash directly to nonunion members who performed bargaining unit work on the mistaken assumption that they were not covered. The trusts, to which the money should have been paid, recovered. The court stated: "The payment of cash to nonunion members, however well-intentioned such payment might have been, does not excuse the obligation to make contributions to the funds . . . the funds are established for the benefit of all employees covered by their language and depleted by the amount which the Rolfsons have refused to contribute."

In *Waggoner* v. *Dallaire*, 649 F.2d 1362 (9th Cir. 1981), a trustee audit revealed delinquencies arising out of an oral modification of a collective bargaining agreement in violation of Section 302(c)(5) of the LMRA. The court enforced the contract as written and also tolled the applicable statute of limitations, noting that the union and the funds were separate entities so that the union's participation in the modification did *not* put the trustees on constructive notice of the employer's failure to contribute. *In accord, Kemmis* v. *McGoldrick*, 706 F.2d 993 (9th Cir. 1983, discussed in Central States' Supplemental Brief).[32]

Finally, access to complete employee records is necessary in all situations involving subcontracting clauses where contributions are claimed *measured by hours worked* by nonunion signatories, *Walsh* v. *Schlecht*, 429 U.S. 401 (1977); *Brogan* v. *Swanson Painting Co.*, 682 F.2d 807 (9th Cir. 1982), or where an issue arises as to whether an individual performing covered work is an "employee" under the NLRA or an independent contractor. *See Teamsters Construction Workers Local 13 Health and Wel-*

[32] See also *Manning* v. *Wiscombe*, 498 F.2d 1311 (10th Cir. 1974), a pre-ERISA case in which the court held that certain funds were entitled to contributions on behalf of nonunion members although the contract had been applied for years on a "members only" basis. Trustee access to complete employee records is particularly important in "right to work" states where bargaining unit employees may enjoy the full benefits of a collective bargaining agreement without joining a union or even paying an agency fee.

fare Trust Fund v. *Hawg N Action*, 651 F.2d 1384 (10th Cir. 1981). These situations are likely to occur particularly in the construction and trucking industries.

In *Nichols* v. *Trustees of Asbestos Workers Local 24 Pension Plan*, 3 EBC 1726 (No. 80-563, D.D.C. 1982), the IRS approved a pension plan amendment that retroactively reduced monthly retirement benefits by one-third. The trustees had presented data indicating that, given the state of the plan's assets as well as its current and future liabilities, the previous level of benefits could not be sustained if the plan were to continue to be funded on an actuarially sound basis as required by ERISA. In the course of a lawsuit subsequently filed by adversely affected retirees, it was established that the Local 24 plan had reciprocal agreements with nine other pension plans. These agreements provided that participants working in covered employment within the jurisdiction of another plan would have their contributions transferred to the plan in which they were participants, in this case, the Local 24 plan. The trustees admitted that they had "little way of knowing when participants are working in other jurisdictions," and that they relied on the participants themselves and on employers to make the appropriate reciprocal contributions. The retirees claimed that the trustees had "breached their fiduciary duty by failing to design and implement an adequate system for identifying and collecting employer contributions" due from plans having reciprocal agreements.

While the court refused to find a breach because the reciprocal plan was relatively new, it stated unequivocally "that it is clearly the duty of the Trustees to determine what is owed to the plan" and "to create a system by which future reciprocal contributions may be monitored, recorded, and credited with accuracy. Anything less would not be what 'a prudent man acting in like capacity and familiar with such matters' would do. ERISA Section 404(a)(1)(B), 29 U.S.C. § 1104(a)(1)(B). How the Trustees fulfill this duty is left to the discretion of the Trustees themselves; the Court, in its limited role in the administration of pension trusts, may only order them to do so."[33]

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[33] *See Waggoner* v. *C & D Pipeline Co.*, 601 F.2d 456, 459 (9th Cir. 1979). Noting "the need for a mechanism to police [compliance with the collective bargaining] agreement" the court stated: "A requirement that contributions be based on all hours worked or paid permits the trustees

(Footnote 33 continued on Page 36)

The Central States Health and Welfare and Pension Funds are not new; they were established, respectively, in 1950 and 1955. As the funds grew in size, it became increasingly necessary to develop systematic methods for enforcing compliance and verifying accuracy. A formal field audit program was therefore instituted based on procedures utilized in the accounting profession and set forth in an audit manual. These procedures have now been refined and set forth in a new and enlarged audit manual. These procedures are themselves expected to develop in accordance with plan experience. In imposing its "limited audit" theory, the Sixth Circuit interfered with "trustee discretion," emasculated the Central States field audit program, and transgressed the "limited role" of courts in the administration of employee benefit trusts. In so doing, the court not only failed to consider the dangers of misreporting in general but, ignored the apparent misreporting of *Central Transport* itself. Refusing to acknowledge the need for the random general audits devised by Central States to effectively monitor *their particular* self-reporting system, the court simply did not give credence to the fact that situations illustrated by the cases set forth above can and do occur although a number of such scenarios were presented to the panel. Substituting its "wisdom" for the "discretion" and experience of the Trustees, without evidence either of the cost of the audit program relative to monies collected, and without an authoritative basis upon which to predicate alternative surveillance schemes, the Sixth Circuit simply dismissed the requested audit as "arbitrary and capricious," imprudent, and a waste of Fund assets. The court's position is belied not only by the facts of *this* case and the cases discussed above; it stands in direct conflict with the approach to Trustee discretion in areas encompassed by ERISA's fiduciary duty provision as articulated in *Nichols* and the circuit decisions cited therein.[34] The Sixth Circuit's "limited audit" theory is clearly erroneous as a matter of practice and precedent.

(Footnote 33 continued from Page 35)
to rely on payroll records to determine if the employers are making the proper contributions to the trust funds." The court did not qualify or otherwise limit the phrase "payroll records."

[34] *Rosen* v. *Hotel and Restaurant Employees, Local 274*, 637 F.2d 592 (3d Cir. 1981); *Nedd* v. *United Mine Workers*, 556 F.2d 190 (3d Cir. 1977), on remand, 506 F. Supp. 891 (M.D. Pa. 1981); *Johnson* v. *Botica*, 537 F.2d 930 (7th Cir. 1976); *Pete* v. *United Mine Workers*, 517 F.2d 1275 (D.C. Cir. 1975).

I.B. Prudence dictates that fund trustees develop independent methods for monitoring employer compliance: reliance on third persons is inconsistent with the spirit of ERISA, the LMRA and case law

One of the most erroneous and harmful aspects of the Sixth Circuit's decision is the court's assumption that the Funds can be adequately protected by the efforts of unions, employees themselves, or the Secretary of Labor. The notion that third persons can and should be relied upon as effective and consistent safeguards to monitor a self-reporting system of collecting revenues and to identify undisclosed plan participants stands in utter opposition to Congress's intent that employee benefit funds should be entirely independent of union control (29 U.S.C. § 186(c)(5), LMRA), that "trustee responsibilities" are nondelegable (29 U.S.C. § 1105, ERISA), that collection actions should be streamlined (126 Cong. Rec. (House) 23039, August 25, 1980), and that it is the function of trustees to protect participants and beneficiaries and not that of beneficiaries to protect the trusts (29 U.S.C. § 1001(a), *et. seq.*).[35]

The court of appeals placed particular reliance on union efforts in monitoring the honor system of reporting and protecting the interests of all eligible participants. Such reliance is inconsistent with decisions of this Court and of the Third, Eighth, and Fifth Circuits. (Petition, 13-15).

In *Schneider Moving & Storage Co., et al.* v. *Robbins, et al., supra*, this Court rejected the argument that unions owe an express or implied statutory or contractual duty of fair representation to benefit fund trustees. Recognizing that unions might be unwilling to expend their limited resources to arbitrate coverage disputes on behalf of trustees without a requirement of reimbursement, or that the union might disagree with the trustees' position and either refuse to arbitrate altogether or compromise the trustees' position in arbitration, which would predetermine the ultimate judicial outcome and hence potentially diminish fund assets, the Court found it *unlikely* that the parties to the Central States Trust Agreements intended to *rely* on the union to arbitrate

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[35] *See United Mine Workers of America Health and Retirement Funds* v. *Robinson*, 455 U.S. 562 (1982); *NLRB* v. *Amax Coal Co.*, 453 U.S. 322 (1981); *Schneider Moving and Storage Co. et al* v. *Robbins, et. al.*, 104 S. Ct. 1844 (1984) and Petition for Certiorari, pp. 12-17.

disputes arising under particular employers' collective bargaining agreements in audit and collection matters (slip. op. pp. 9-11). Hence, direct access by the Trustees to federal courts was approved, consistent with the *en banc* opinion of the Eighth Circuit, 700 F.2d 433 (8th Cir. 1983).

The Third Circuit addressed and rejected the "fair representation" argument specifically in the context of surveillance strategies. In *Rosen* v. *Hotel and Restaurant Employees, Local 274*, 637 F.2d 592 (3d Cir. 1981), the court stated that fund trustees, not unions, have a fiduciary duty to "oversee" employer contributions: "While the union does owe a duty of fair representation to its members (citations omitted), it does not control, nor is it in a position to oversee, the employer's contributions to the fund" (p. 599, fn. 10).[36]

Even if unions were in a position to "oversee" employer reporting, the duty of fair representation to the bargaining unit as a whole might prompt them not to press claims for fringe benefits if this jeopardized base wages or jobs. As this Court noted in its *Schneider* opinion, *supra:*

> Even if there were a duty of fair representation here, it would accord the union wide discretion and would provide only limited protection to trust beneficiaries. A primary union objective is "to maximize overall compensation of its members." *Barrentine* [v. *Arkansas-Best Freight System*], 450 U.S., at 742. Thus, it may sacrifice particular elements of the compensation package "if an alternative expenditure of resources would result in increased benefits for workers in the bargaining unit as a whole." *Id* (slip. op., pp. 11-12, fn. 22).

Although the Court here addressed the union's duty of fair representation in the context of a purported duty to arbitrate coverage disputes on behalf of benefit fund trustees, the reasoning applies with equal force to a purported duty on the part of a union to monitor a *fund's* self-reporting system. As observed in *Barrentine, supra, collective* bargaining and the duty of fair representation under the LMRA are not necessarily consistent with the protection of *individual* rights, particularly individual *statutory* rights. To the

[36] Like the Trustees, unions may also be *physically* unable to monitor reporting at every employer's facility in their jurisdiction every month.

extent that the Sixth Circuit limited the scope of the Trustees' audit in reliance on the union to protect the benefit rights of all covered employees, the decision was clearly erroneous.

The court also believed that employees could pursue their own benefit rights, suggesting that they might be estopped from claiming them if they did not.

The Third Circuit expressly repudiated such a proposition in *Rosen* v. *Hotel and Restaurant Employees, Local 274, supra*, and forced a fund to grant a participant his benefits even though the employer did not contribute appropriately and even though the district court, in denying the pension claim, had "emphasized that Rosen was indifferent and pressured neither the Trustees, the employer nor the union to secure the contributions" (637 F.2d at 596). *See also Pacific Iron & Metal Co.* v. *Western Conf. of Teamsters Pension Trust Fund*, 553 F. Supp. 523 (W.D. Wash. 1982), in which the court stated that an employee decision to decertify the union did not constitute a voluntary waiver of pension rights.

Finally, the court of appeals suggests that the Secretary of Labor can aid the funds. Neither the legislative history of ERISA nor the text of the statute supports the idea that the Secretary's investigative activity comprehends random general audits similar to those performed routinely by the Administrator of the Wage and Hour Division of the Department of Labor under the Fair Labor Standards Act (29 U.S.C. § 211). Thus, ERISA does not authorize the Secretary *to enter* an employer's premises and inspect books and records unless he has reasonable cause to believe a violation of the statute has occurred (29 U.S.C. § 1134).[37] Even with reasonable cause, the Secretary's investigative activity is discretionary. Given the large number of employers contributing to employee benefit plans and the manpower available to the DOL, history and logic suggest that the Secretary's intervention will be reserved for unusual situa-

[37] "Reasonable cause" is required only for *physical entry*, not for DOL requests for the production of records at its offices. Clearly, the more limited in scope a trustee audit is, the less is the ability of a fund to detect discrepancies and hence to provide the DOL with "reasonable cause" to conduct a more substantial on-site investigation. This applies *a fortiori* to anyone else who might request a DOL audit. In any event, the government concedes that routine employer audits would impose a great burden. (*See* United States' Brief in Support of Petition, p. 19.)

tions. In fact, it appears that the major focus of DOL investigative activity has been and will continue to be plans themselves and their trustees. CCH Pension Plan Guide ¶ 25,496 (May 19, 1983). As the Eighth Circuit observed in *Robbins* v. *Prosser*, 700 F.2d at 422:

> Defendants suggest that the trustees, in addition to asking the union to invoke arbitration, could also seek administrative or criminal remedies, but these avenues are even more remote and uncertain than the second-hand access to arbitration that is put forward as the funds' main recourse.

Significantly, in enacting the MEPPAA, Congress *withdrew* from the Secretary his power to institute a collection action (29 U.S.C. §§ 1132(b)(2), 1145). Any implication that the Funds can rely on the DOL to conduct random, routine field audits is clearly erroneous.

I.C. Prudence dictates that the Central States Trustees maintain a vigorous field-audit program as an "internal control" which is relied upon by its independent CPA in certifying the Funds' annual financial reports prepared

ERISA requires employee benefit funds to file detailed annual financial reports in accordance with generally accepted accounting principles which assure that the information contained therein presents a fair and accurate picture, most importantly, of the plan's liabilities and net assets available to pay plan benefits.[38] This report must, in turn, be verified by an independent certified public accountant after himself examining the plan's books, records, other supporting documentation, and internal controls in accordance with generally accepted auditing standards.

In accordance with FASB No. 35, two of the most critical foci of independent investigation are the plan's participant data and contributions received or receivable. In assessing a plan's financial statements, an independent auditor generally looks first to the plan's internal accounting controls, for example, its record-keeping, verification, bill-

[38] *See Audits of Employee Benefit Plans*, American Institute of Certified Public Accountants, 1983; Financial Accounting Standards Board (FASB) Statement No. 35, *Accounting and Reporting by Defined Benefit Pension Plans* (March, 1980). The primary objective of a plan's financial statements is to present information that is useful in assessing the plan's present and future ability to pay benefits when due.

ing, claims processing, and disbursements mechanisms.[39] A field audit program to verify the accuracy of participant data and contributions is regarded as an important "internal control." If the procedures used by the plan's internal auditors comply with generally accepted auditing standards, the independent auditor may feel he can rely on this control for assessing the general accuracy of employer reporting and thus limit his own field testing. Conversely, if audits of contributing employers are not performed by a plan or the independent auditor is not satisfied with the audit results, he may find it necessary to take to the field himself and examine the records of selected employers.[40]

Arthur Young and Co. is the independent auditor of Central States' annual financial reports. The company has filed Amicus Briefs, which set forth the opinion of professionals in the field. It is clear that Arthur Young does not regard an audit of the records of concededly covered employees as an inquiry comporting with generally accepted auditing standards. This is because such an audit deprives the auditors from *independently* verifying the accuracy or completeness of the employer's representations.[41] Hence, limited audits cannot serve as a reliable internal control. Conversely, the existence of a vigorous field audit program, governed by generally accepted auditing procedures that permit access to pertinent records encompassing a complete "employee universe," does serve as a reliable internal control which in turn creates a reasonable belief that, viewing the plan as a whole, participants have been correctly reported and contributions accurately made and that the plan's financial statements present a fair and accurate picture of its ability to pay benefits (providing that the plan's internal mechanisms for processing the data are also satisfactory).

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[39] *See* detailed checklist in Gilbert, Lachowicz, and Zid, *Accounting and Auditing for Employee Benefit Plans* (Warren, Gorham & Lamont: New York and Boston, 1978), Chapter 14.

[40] *See Gilbert*, et al., *Accounting and Auditing for Employee Benefit Plans*, *supra*, Chapter 15, for suggested procedure in testing employer records for accurate reporting.

[41] *See* AICPA, Statement on Auditing Standards No. 39 § 17, AU 350.17. "An Auditor would not be able to detect understatements of an account due to omitted items by sampling the recorded items. An appropriate sampling plan for detecting such understatements would involve selecting from a source in which the omitted items are included.

As noted above, Central States maintains a sizeable audit staff, comprised primarily of CPAs who have been trained to examine employer records in accordance with generally accepted auditing standards. Arthur Young approves of this internal control, clearly believing that it encourages correct reporting, deters evasions, and permits the Trustees to have better knowledge of the Funds' assets and liabilities in the interests of participants and beneficiaries. It would be *imprudent* to fail to defend or to weaken an established practice which has been endorsed by the Plans' independent auditor and contributes to the preservation of Central States' tax-exempt status.[42]

Both pre-ERISA and post-ERISA law is well-established that reviewing courts may not substitute their own judgment for that of benefit fund trustees or interfere with their decisions unless these decisions are "arbitrary and capricious." *Danti* v. *Lewis*, 312 F.2d 345 (D.C. Cir. 1962); *Rehmar* v. *Smith*, 555 F.2d 1362 (9th Cir. 1976). For trustees' conduct to qualify as "arbitrary and capricious," however, the act or decision must lack substantial justification, have no basis in fact, be erroneous as a matter of law, be inconsistent, or be made in bad faith.[43]

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[42] If Central Transport prevails, the Trustees will have no alternative but to initiate lawsuits to compel the production of records through discovery. This will place a serious burden on fund assets as well as on the federal courts. There is little litigation on this subject. However, the Seventh Circuit, in an unreported decision, stated that a request for discovery is different from a request to compel a complete audit on the merits. *See Central States, Southeast and Southwest Areas Pension Fund, et al.* v. *Hribar Trucking*, No. 81-2422 (June 16, 1982). Should other courts, however, decide that funds may not obtain through discovery what they are not entitled to on the merits, a new privilege for employee records will have been created that is not found in the Federal Rules of Evidence. This Court has expressly rejected the creation of new privileges under Rule 501 of the Federal Rules of Evidence where the effect of such privileges will obstruct lawful and necessary discovery. *See U.S.* v. *Arthur Young*, No. 82-687 (March 21, 1984). (No accountant-client privilege for tax-accrual work papers, even though these papers contain the accountant's *confidential opinions* on *possible* IRS positions with regard to the taxpayer.)

[43] These qualifications are legion in circuit decisions. By way of example, *see Marsh* v. *Greyhound Lines, Inc.*, 488 F.2d 278 (5th Cir. 1974); *Maness* v. *Williams*, 513 F.2d 1264 (8th Cir. 1975); *Adams* v. *N.J. Brewery Employees Pension Trust Fund, et al.*, 670 F.2d 387 (3d Cir. 1982); *Wardle* v. *Central States, Southeast and Southwest Areas Pension*

(Footnote 43 continued on Page 43)

The court of appeals did substitute its judgment for that of the Trustees. Without showing that random general audits were arbitrary and capricious as qualified by a majority of other courts, it created a *particularized* "reasonable cause" standard for the production of documents based on its own narrow view of relevance. For all the reasons set forth above, the court's departure from the traditional method of reviewing discretionary trustee activity and its interpretation of the "prudent man" rule of ERISA are clearly erroneous.

II. THE TRUSTEES' NEED FOR INFORMATION OUTWEIGHS THE EMPLOYER'S INTEREST IN CONFIDENTIALITY: A REVIEW OF THIS DEFENSE TO DISCLOSURE IS AS NECESSARY IN THE CONTEXT OF ERISA AS IT WAS IN THE CONTEXT OF THE NATIONAL LABOR RELATIONS ACT

The thesis of Petitioners' argument, in a nutshell, is that audits must be independent if they are to serve as a reliable tool for verifying representations made by the subject of the inquiry. Governmental agencies, in particular the IRS, have been granted—both by the legislature and the judiciary—great investigative latitude commensurate with the public interests at stake.[44] Fund trustees serve an analogous public interest, namely, "the continued well being and security of millions of employees and their dependents" (29 U.S.C. § 1001). They, too, require investigative latitude. However,

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(Footnote 43 continued from Page 42)

Fund, 627 F.2d 820 (7th Cir. 1980). Although these decisions have emerged mainly in the area of benefit claims, where courts have scrutinized trustees' interpretations of plan documents, there is no authority to suggest that acts or decisions undertaken by trustees pursuant to the "prudent man" rule of ERISA should be more stringently reviewed *as long as* the trustees are acting *solely* in the interests of participants and beneficiaries. *See Struble, et al.* v. *New Jersey Brewery Employees' Welfare Trust, et al.*, No. 83-5115, et al. (3d Cir. April 16, 1984); *see also Nichols* v. *Trustees of Asbestos Workers Pension Plan*, 3 EBC 1726 (D.D.C. 1982). This approach would be consistent with the common law basis of the rule.

[44] Confidentiality arguments carried little weight in *U.S.* v. *Arthur Young, supra*, in which the Court rejected an accountant-client privilege. *See also Donaldson* v. *U.S.*, 400 U.S. 517 (1971), in which the Court stated that a taxpayer had *no proprietary interest in his employment and compensation records* such that he could prevent their production to the IRS pursuant to a summons issued to his former employer under 26 U.S.C. § 7602.

because they are private individuals, ultimately gathering information for private funds, confidentiality concerns arise which are not present in agency-initiated audits. Hence, competing needs must be accommodated.

While a balancing of competing interests has led to the emergence of well-defined rules for the disclosure of confidential information to unions in order to enable them to effectively perform their role as bargaining representatives, this technique has not yet led to equivalent disclosure standards where benefit fund trustees request information under the authority of ERISA in order to effectively perform their role as prudent fiduciaries. Nevertheless, the district court accepted, as an appropriate analogy, the relevance standards enunciated by this Court and the courts of various circuits in 8(a)(5) refusal to bargain cases, and found that on balance the Trustees' interest in verifying information on employment status through random general audits outweighed the employer's interest in protecting the confidentiality of records, given the safeguards offered by the Central States Funds to protect that interest.

The court of appeals accepted the NLRB disclosure rules analogy only with reluctance, and then found that Petitioners did not satisfy the relevance test or protect the interests of Transport or its noncovered employees. Misconstruing the purpose of the audit as a strategy "triggered" by reporting inaccuracies, the court found that "concern over the status of four employees" did not "justify an investigation into the records of all Transport's employees". As observed above, the court inexplicably failed to recognize that these findings were the *result* of the audit not its precipitating cause. Moreover, it did not even *once* address the safeguards *offered* to protect the interests of Transport and its employees, let alone decide whether such safeguards were sufficient and should be considered as part of a balancing test.

The key to disclosure in NLRB decisions is relevance. *See Curtiss-Wright* v. *NLRB*, 59 L.R.R.M. 2433 (3d Cir. 1965). Webster's and Oxford define "pertinent" as "relevant" to the matter at hand. The Trustees have shown why access to "pertinent" records beyond those of "concededly covered employees" is "relevant" to a "prudent" inquiry. The Sixth Circuit's *particularized* "reasonable cause" stan-

dard for random Trustee audits is utterly inconsistent with the liberal "discovery-type" standard of relevance and hence disclosure approved by this Court in *NLRB* v. *Acme Industrial Co.*, 385 U.S. 432 (1967). It is also inconsistent with the balancing process undertaken by the Court in *NLRB* v. *Detroit Edison*, 440 U.S. 301 (1979), discussed in the Petition at pp. 24-25.

Detroit Edison suggests that the greater the sensitivity of the information requested, the greater is the interest in confidentiality. Nevertheless, the Court did not give its approval to a naked assertion of confidentiality. If information is relevant, it must be produced in some useful form. Moreover, consent to the release of allegedly confidential information, even of a highly sensitive nature, is not a *per se* requirement for its disclosure. Rather, consent would appear to depend on the burden of obtaining it and on whether an express promise not to disclose was made.

In the case at bar, the court of appeals accepted Transport's assertion of confidentiality with regard to an alleged majority of its employees, although no alternatives were offered to permit independent verification of the accuracy of reporting, although the burden on the trustees of obtaining consent from these employees would have been onerous, if not impossible, although the materials requested were not of the same degree of sensitivity as aptitude tests and test scores, and although more than a quarter of a million dollars of alleged delinquencies were determined for the concededly covered group before the auditors were asked to leave the premises.

The Trustees have offered specific and substantial safeguards to protect confidentiality. See Petition at pp. 25-26 and App. I P.C. These safeguards can be monitored by the employer. Moreover, if this information is "leaked" to promote union-organizing efforts or the competitive interests of rival employers (specters which Transport raised without a shred of evidence to show that the Trustees have *ever* transmitted audit results for such purposes), this would be not only a breach of the strict neutrality rule set forth by this Court in *NLRB* v. *Amax Coal Co.*, *supra*, it would also be a breach of the Trust Agreements and Fund policy and hence remediable in a judicial proceeding. More to the point: fund trustees have a *practical stake* in promoting

confidentiality so as to assure the continued cooperation of employers in monitoring a self-reporting system from which employers themselves stand to benefit. *See U.S.* v. *Bisceglia*, *supra*.

Before now, this Court has enhanced the union's ability to perform its statutory duty by fashioning standards of relevance and articulating disclosure rules in the context of collective bargaining; it has done so by balancing competing interests. Petitioners now request this Court to undo the *de facto* privilege created by the court of appeals, and enhance the ability of fund trustees to perform their fiduciary obligations through a similar process of balancing.

III. THE TRUST AGREEMENTS GOVERNING THE CENTRAL STATES FUNDS PROVIDE A CONTRACTUAL BASIS FOR RANDOM GENERAL AUDITS

In conducting random general audits, Petitioners have consistently relied on Article III, Section 5, *sentence two* of the Trust Agreements. This provision states:

> The Trustees may, by their representatives, examine the *pertinent records* of each Employer at the Employer's place of business whenever such examination is deemed necessary or advisable by the Trustees in connection with the proper administration of the Trust (App. F P.C., A 46, emphasis added).

Exercising their power to construe the terms of the Trust Agreements, and to make these constructions binding on employers, employees, and the union (Article IV, Section 17, App. F P.C., A 48), the Trustees have consistently and at all stages of this litigation urged that the term "pertinent records" means records necessary to complete the audit in accordance with recognized procedures which require independent verification of employer representations. At a minimum, this construction could *reasonably* include records beyond those of employees the *employer* concedes are covered. Indeed, in its *Schneider* opinion, *supra*, this Court noted, quoting Article III, Section 5, *sentence two*, of the Trust Agreements: "To ensure compliance with the contribution requirements, the trust agreements gave the trustees the authority to examine petitioners' payroll records" (slip. op., p. 5). The Court did not *qualify* the phrase "payroll records."

The district court upheld the Trustees' construction; the court of appeals reversed, finding that the term "pertinent records" was synonymous with the term "employee records."[45] In reaching this conclusion, the court first of all substituted the term "employee records" for the term "pertinent records," in effect *rewriting an express* provision of the Trust Agreements. It also rejected the Trustees' reasonable construction of the term "employee," which encompasses not only the "concededly covered" group but also the "*de facto* covered" group which the court itself agreed could sustain a claim for benefits, *regardless of concession*, in a court or through arbitration (App. B P.C., A 29).[46]

As Central States argued in the Petition for Rehearing *en banc* (pp. 7-9), the Trustees *have never asserted* that the term "employee" as used in the Trust Agreements means "covered and noncovered employee" (*id.*, A-24/25). They cannot, by law, extend "coverage" under the labor agreement, "rights" under the Trust Agreements, or "benefits" in the Funds to "noncovered employees." What the Trustees *do claim* is that they have a nondelegable duty under 29 U.S.C. §§ 1104 and 1105 to look beyond lists and records of "*concededly* covered employees" in order to verify that an employer is accounting for *all covered employees* in its work force (conceded and *de facto*), particularly since it is the Funds which bear ultimate financial liability to any employee who can sustain a claim for benefits on the basis of covered employment actually performed *regardless* of whether contributions were ever or can ever be received on

[45] Article I, Section 3(a) of the Trust Agreements defines the term "employee" as one covered by the collective bargaining agreement and eligible for contributions under the contract or applicable law (App. F P.C., A 43). Article III, Section 5, sentence two *expressly does not* limit the production of records for audit purposes to those of "employees," no less to those of "concededly covered employees:" it specifies "pertinent records."

[46] Focusing on the definition of "employee" in Article I, Section 3(a), the court reasoned that if the term "employee" is construed to include "noncovered" as well as "covered" employees, then the Trustees would not only be entitled to examine the records of "noncovered" employees but would also have to extend rights and benefits under the trusts to "noncovered" employees which would be contrary to the intent of the parties to the Trust Agreements as well as to the collective bargaining agreements. It would also be contrary to ERISA, which requires fund trustees to exercise their fiduciary obligations solely to participants and beneficiaries (*id.*, A-19; 24-25).

his behalf. In this regard, Petitioners point out the obvious: while nonparticipants and nonbeneficiaries *are* admittedly outside the scope of the Trustees' fiduciary duty, undetected "covered" employees are not nonparticipants. Properly construed, the Trust Agreements are clearly *consistent* with ERISA. *See* 29 U.S.C. § 1104(a)(1)(D). 29 U.S.C. § 1002(7) defines "participant" as an "employee" who is or "may become" eligible for benefits.

In rejecting the Trustees' contractual claim, the panel departed from the limited standard of judicial review set forth above in connection with ERISA. The decision is therefore in direct conflict with *Riley* v. *MEBA Pension Trust*, 570 F.2d 406 (2d Cir. 1977), in which the court asserted that where a trust agreement affords trustees broad powers of construction, "the judicial role is limited to determining whether the trustees' interpretation was made rationally and in good faith, not whether it was right." This Court, in its *Schneider* opinion, *supra*, also accorded great weight to the Trust Agreements, noting that any good faith interpretation thereof by the Trustees would be binding. The Trustees' construction of "pertinent records" in the case at bar comports with good faith and audits conducted in accordance with generally accepted standards are surely within the scope of their authority. The court of appeals' interpretation of the Trust Agreements as well as its standard of review of the Trustees' construction is clearly erroneous.

CONCLUSION

The court of appeals' decision has placed the trustees of multiemployer employee benefit funds in an untenable position: they must shoulder their fiduciary responsibilities independently but are urged to rely on the discretionary activity of Unions and the Secretary of Labor who may be moved by competing interests of their own and over whom the trustees have no control; they must exercise these fiduciary obligations solely on behalf of participants and beneficiaries but are urged to rely on the very people whose interests they are supposed to protect; they must

disclose information to plan participants whose identity they cannot necessarily ascertain; they must protect the actuarial solvency of the funds but cannot fully oversee employer contributions; they must grant credits and benefits to employees on the basis of covered employment but cannot fully verify coverage in advance of claims made; they must conserve fund assets but are faced with the possibility of conducting multiple law suits in order to pursue a routine matter of trust administration.

For all of the reasons set forth herein, Petitioners respectfully request this Court to reverse the decision of the Sixth Circuit; to affirm the decision of the district court; to give content to the prudent man and fiduciary duty rules of ERISA; to articulate a uniform standard for the judicial review of trustee actions; to establish an appropriate standard of relevance and hence appropriate disclosure rules for the production of documents to trustees; and to reconfirm the principles of nondelegability and trustee independence.

Respectfully submitted,

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August 9, 1984

NO. 82-2157

In the

Supreme Court of the United States

October Term, 1983

CENTRAL STATES, SOUTHEAST AND SOUTHWEST AREAS PENSION FUND and CENTRAL STATES, SOUTHEAST AND SOUTHWEST AREAS HEALTH AND WELFARE FUND,
Petitioners,

v.

CENTRAL TRANSPORT, INC., et al.,
Respondents.

PETITIONERS' APPENDIX

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APPENDIX A

Petitioners' Complaint

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

CENTRAL STATES, SOUTHEAST AND SOUTHWEST AREAS PENSION FUND and CENTRAL STATES, SOUTHEAST AND SOUTHWEST AREAS HEALTH AND WELFARE FUND,

Plaintiffs,

vs. Case No.

CENTRAL TRANSPORT, INC., a Michigan corporation; CENTRAL CARTAGE CO., a Michigan corporation; GENESEE CARTAGE CO., a Michigan corporation; QUAD STATE LEASING, INC., a Michigan corporation; CADILLAC LEASING, INC., a Michigan corporation; DUNES LEASING, a Michigan corporation; CENTRAL RECAPPING, INC., a Michigan corporation; MICHIANA TRUCKING, INC., a Michigan corporation; COMPANY 17, DANVILLE ILLINOIS LEASING, MICHIGAN EXPRESS, MOHAWK CARTAGE, MOHAWK MOTOR, INC., FLINT CARTAGE, BANCROFT FREIGHT LINES, and MCKINLEY TRANSPORT, LIMITED,

Defendants.

COMPLAINT

NOW COME the Plaintiffs, by their attorneys, Russell N. Luplow and Charles J. Taunt, Of Counsel, and as and for a cause of action against the Defendants allege and show to the Court as follows:

1. Jurisdiction of this Court is founded upon: Section 301(a) of the Labor Management Relations Act of 1947, as

amended, (29 USC Section 185(a)); and Section 502 of the Employee Retirement Income Security Act of 1974, (29 USC 1132) in that the Plaintiffs are aggrieved by the Defendants' violation of a collective bargaining agreement, Trust Plan and Trust Agreement and the Defendants' continued refusal to comply with certain terms of a collective bargaining agreement and the Trust Plan and Trust Agreement of the Central States, Southeast and Southwest Areas Pension Fund and the Central States, Southeast and Southwest Areas Health and Welfare Fund thereby violating the provisions of the Employee Retirement Income Security Act of 1974 and the terms and provisions of said employee benefit plans, Section 301 of the Labor Management Relations Act of 1947 and the Common Law of the State of Michigan.

2. Plaintiff, Central States, Southeast and Southwest Areas Pension Fund is an employee benefit plan, within the meaning of Sections 3(1)(2)(3)(21), 405(C)(1)(B) and 502 of the Employee Retirement Income Security Act of 1974 (29 USC 1002(1)(2)(3)(21), 1109(C)(1)(B) and 1132) and brings this action on behalf of the Trustees, participants and beneficiaries of said Plan. The Central States, Southeast and Southwest Areas Pension Fund maintains offices and its principal place of business in a state other than the State of Michigan, to-wit: 8550 West Bryn Mawr Avenue, in the City of Chicago, County of Cook, State of Illinois and is a citizen of the State of Illinois.

3. Plaintiff, Central States, Southeast and Southwest Areas Health and Welfare Fund is an employee benefit plan, within the meaning of Sections 3(1)(2)(3)(21), 405(C)(1)(B) and 502 of the Employee Retirement Income Security Act of 1974 (29 USC 1002(1)(2)(3)(21), 1109(C)(1)(B) and 1132) and brings this action on behalf of the Trustees, participants and beneficiaries of said plan. The Central States, Southeast and Southwest Areas Health and Welfare Fund maintains offices and its principal place of business in a state other than the State of Michigan, to-wit: 8550 West Bryn Mawr Avenue, in the City of Chicago, County of Cook, State of Illinois and is a citizen of the State of Illinois.

4. Defendants, Central Transport, Inc., Central Cartage Co., Genesee Cartage Co., Quad State Leasing, Inc., Cadillac Leasing, Inc., Dunes Leasing, Central Recapping, Inc., and Michiana Trucking, Inc. are corporations organized and existing under the laws of the state of Michigan.

5. Defendants, Company 17, Danville Illinois Leasing, Michigan Express, Mohawk Cartage, Mohawk Motor, Inc., Flint Cartage and Bancroft Freight Lines are, upon information and belief, corporate entities organized and existing pursuant to the laws of a state which is unknown to Plaintiffs.

6. Defendant McKinley Transport, Limited is a corporation organized and existing under the laws of the province of Ontario, Canada and is duly authorized to transact business within the state of Michigan.

7. Defendants, Central Transport, Inc., Genesee Cartage Co., Quad State Leasing, Cadillac Leasing, Inc., and Dunes Leasing maintain offices and a place of business within the State of Michigan, to-wit: 34200 Mound Road, Sterling Heights, Michigan 48077 and are citizens of the State of Michigan.

8. Defendant, Central Recapping, Inc., maintains offices and a place of business within the State of Michigan, to-wit: 6419 East Ten Mile Road, Warren, Michigan and is a citizen of the State of Michigan.

9. Defendant, Central Cartage Co., maintains offices and a place of business within the State of Michigan, to-wit: 3399 East McNichols, Detroit, Michigan and is a citizen of the State of Michigan.

10. Defendant, Michiana Trucking, maintains offices and a place of business within the State of Michigan, to-wit: 4570 Sterns, Lambertville, Michigan 48044 and is a citizen of the state of Michigan.

11. Defendants, Company 17, Danville Illinois Leasing, Michigan Express, Mohawk Cartage, Mohawk Motor, Inc., Flint Cartage and Bancroft Freight Lines, maintain offices and a place of business within the state of Michigan, to-wit: 34200 Mound Road, Sterling Heights, Michigan 48077 and are citizens of a state which is unknown to Plaintiffs.

12. Defendant, McKinley Transport, Limited, maintains offices and a place of business within the state of Michigan, to-wit: 34200 Mound Road, Sterling Heights, Michigan 48077 and is a citizen of the Province of Ontario, Canada. McKinley Transport Limited engages in business within the state of Michigan.

13. Defendants are engaged in the business of the transportation of goods in interstate commerce as common carriers.

14. Defendants are employers and parties in interest in an industry affecting commerce within the meaning of Section 3(5)(11)(12) and (14) of the Employee Retirement Income Security Act of 1974 (29 USC 1002(5)(11)(12) and (14)) and Labor Management Relations Act of 1947 (29 USC 151 *et seq.*).

15. For all times relevant herein, Defendants were parties to and agreed to abide by the terms of collective bargaining agreements between themselves and various Local Teamster Unions who are labor organizations that represent for purposes of collective bargaining, certain employees of Defendants and employees of other employers in industries affecting interstate commerce within the meaning of Sections 2(5), 9(a), and 301(a) of the Labor-Management Relations Act of 1947, as amended (29 USC 151, *et seq.*).

16. The executed collective bargaining agreements described herein contain provisions whereby Defendants agreed to make timely payments to Plaintiffs' trust funds for each employee covered by said agreement. By execution of said collective bargaining agreements, the Defendants authorized the employers associations which are parties thereto to enter into appropriate trust agreements necessary for the administration of Plaintiff Funds and to designate the employer trustees under such agreement, thereby waiving all notice and ratifying all actions taken or to be taken by the trustees within the scope of their authority.

17. Defendants have executed Participation Agreements (applicable to the Pension Fund) and Joint Applications

(applicable to the Health and Welfare Fund) wherein they agreed to be bound by and assented to all of the terms of the Trust Agreement creating the respective Funds and all of the rules and regulations theretofore and thereafter adopted by the Trustees of said trust funds pursuant to said trust agreements and all action of the trustees in administering such trust funds in accordance with the trust agreements and rules adopted.

18. By executing said Participation Agreements and Joint Applications Defendants agreed to make timely payments to Plaintiffs' trust funds and to designate as their representatives such trustees as are named in the trust agreement together with their successors.

19. Defendants have failed to perform their obligations pursuant to the terms and conditions of the collective bargaining agreements, participation agreements, joint applications and trust agreements for the Pension and Health and Welfare Funds including but not limited to the following:

a. Failure to make continuing and prompt payments to the Plaintiff Pension and Health and Welfare Funds as required by the applicable collective bargaining agreements, participation agreements, joint applications and trust agreements between the parties;

b. Failure to furnish to the Plaintiffs' trustees, upon reasonable demand, the names, current addresses, social security numbers and hours worked by each employee.

c. Failure to accurately report employee work status to Plaintiffs.

d. Failure to permit Plaintiffs' representatives to complete an examination of the pertinent records of each Defendant at said Defendant's place of business, despite Plaintiffs' request to do so.

20. Plaintiffs' trust agreements provide at Article III, Section 5:

> Production of Records. Each Employer shall promptly furnish to the Trustees, upon reasonable demand, the names and current addresses of its Employees, their Social Security numbers, the hours worked by each Employee and such other information as the Trustees

may reasonably require in connection with the administration of the Trust. The Trustees may, by their representatives, examine the pertinent records of each Employer at the Employer's place of business whenever such examination is deemed necessary or advisable by the Trustees in connection with the proper administration of the Trust . . .

21. Plaintiffs are informed and believe that for a substantial period of time, the exact dates being unknown to Plaintiffs, Defendants have employed numerous persons pursuant to the within-referenced collective bargaining agreements for whom Defendants have failed to accurately report the true employment status to Plaintiffs and on whose behalf Defendants have failed to remit the required contributions to Plaintiffs.

22. On February 4, 1980, Plaintiffs, by their duly authorized representatives, commenced an audit of the pertinent records of Defendants.

23. Plaintiffs continued to conduct an audit of Defendants' records until March 28, 1980.

24. On March 28, 1980 Defendants directed Plaintiffs' representatives to cease their audit as of the close of business on that date and vacate Defendant's premises. From and after said date Defendants have refused to permit Plaintiffs' representatives to continue an audit and review the pertinent records of Defendants.

25. Defendants' actions in refusing to permit Plaintiffs' representatives to continue an audit and review Defendants' pertinent records constitute a violation of the applicable provisions of the within-referenced collective bargaining agreements, participation agreements, joint applications, trust agreements, and the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1001, *et seq.*)

26. Upon information and belief, Defendants are indebted to Plaintiffs for certain monies, the exact amounts of which are unknown to Plaintiffs at this time.

27. Plaintiffs are unable to determine the exact amount of contributions which may be owing from Defendants to Plaintiffs unless Defendants are compelled by this Court to furnish Plaintiffs with the names, addresses, social security

numbers and hours worked by each employee and permit Plaintiffs' representatives to examine the pertinent records of Defendants and conduct an audit to determine and verify which individuals have been employed by Defendants pursuant to the within-referenced collective bargaining agreements and accurately determine their work status.

28. Plaintiffs have no adequate remedy at law for Defendants' refusal to comply with the terms, conditions, rules and regulations governing Plaintiffs' Trust Funds, and unless the Defendants are enjoined from breaching and continuing to breach the terms of the collective bargaining agreements, participation agreements, joint applications, Trust Plans and Trust Agreements and mandatorily compelled to coply with said documents, Plaintiffs and their Trustees will suffer irreparable harm.

29. The applicable collective bargaining agreements between Defendants and the various local teamster unions include provisions that employers who are delinquent in Pension and Health and Welfare contributions to Plaintiffs must also pay all attorneys' fees and costs of collection of those delinquent contributions.

30. Plaintiffs' Pension Trust Agreement provides, *inter alia*, pursuant to Article XIV, Section 4, and Plaintiffs' Health and Welfare Trust Agreement provides, *inter alia*, pursuant to Article XI, Section 4, that:

> Non-payment by an Employer of any moneys due shall not relieve any other Employer from his obligation to make payment. In addition to any other remedies to which the parties may be entitled, an Employer shall be obligated to pay interest at the rate of nine (9%) percent per annum on the moneys due to the Trustees from the date when the payment was due to the date when the payment is made, together with all expenses of collection incurred by the Trustees, including, but not limited to, attorneys fees and such fees for late payment as the Trustees determine as permitted by law.

31. Section 502(g) of the Employee Retirement Income Security Act of 1974 (29 USC 1132(g)) provides that:

> In any action under this title by a participant, beneficiary, or fiduciary, the Court, in its discretion may

allow a reasonable attorneys fee and costs of action to either party.

32. Pursuant to the above-cited contractual and statutory provisions, Defendants are indebted to Plaintiffs, in addition to such sums as may be found to be due and owing from Defendants to Plaintiffs for delinquent contributions and interest thereon, such additional costs as may be incurred by Plaintiffs for actual attorney fees and expenses of collection incurred by them for recovery of the delinquent contributions described herein.

WHEREFORE, Plaintiffs demand the following relief:

1. An order to show cause why Defendants should not be enjoined from violating the terms of the collective bargaining agreements, participation agreements, joint applications, Trust Plans and Trust Agreements.

2. A Preliminary Injunction enjoining Defendants from violating the terms of the collective bargaining agreements, Participation Agreements, Joint Applications, Trust Plans and Trust Agreements and further directing Defendants to permit Plaintiffs' representatives to conduct an audit and examine the pertinent records of each Defendant at the Defendant's place of business and to provide representatives of Plaintiffs with the names, current addresses, and social security numbers of its employees and the hours worked by each employee together with such documentation as may be required by Plaintiffs' representatives to verify said information.

3. A permanent injunction upon hearing of this cause, enjoining the Defendants from violating the terms of the collective bargaining agreements, participation agreements, joint applications, Trust Plans and Trust Agreements and from disposing of any assets until the terms of the collective bargaining agreements, and Trust Agreements are complied with.

4. A judgment on behalf of Plaintiff, Central States, Southeast and Southwest Areas Pension Fund for such amounts as may be determined to be due and owing from Defendants to Plaintiffs together with accumulated interest thereon from the respective due dates of such contributions,

costs incurred by Plaintiffs in collecting such contributions, actual attorneys' fees and costs of this action, and for such amounts as become due during the pendency of this proceeding.

5. A judgment on behalf of Plaintiff, Central States, Southeast and Southwest Areas Health and Welfare Fund for such amounts as may be determined to be due and owing from Defendants to Plaintiff together with accumulated interest thereon from the respective due dates of such contributions, costs incurred by Plaintiff in collecting such contributions, actual attorneys' fees and costs of this action, and for such amounts as become due during the pendency of this proceeding.

6. That the court retain jurisdiction of this cause pending compliance with its orders.

7. For such other, further or different relief as the Court may deem just and proper.

(s) Russell N. Luplow
Attorney for Plaintiffs
525 Woodward, Suite 1400
Bloomfield Hills, MI 48013

Of Counsel:
(s) Charles J. Taunt
Attorney for Plaintiffs
525 Woodward, Suite 1400
Bloomfield Hills, MI 48013

APPENDIX B
Central States' Audit Engagement Letter

CENTRAL STATES
SOUTHEAST AND
SOUTHWEST AREAS
HEALTH AND WELFARE AND PENSION FUNDS

November 5, 1979 CERTIFIED MAIL

Mr. Robert Sigler
Centra, Incorporated
34200 Mound Road
Sterling Heights, Michigan 48077

RE: CONTRIBUTIONS TO CENTRAL STATES,
SOUTHEAST AND SOUTHWEST AREAS
HELATH AND WELFARE AND PENSION FUND
FOR THE FOLLOWING COMPANIES:

BANCROFT FREIGHT
ACCOUNT NO.: 0566100-0203
CENTRAL CARTAGE
ACCOUNT NO.: 1392300-0300
CENTRAL TRANSPORT
ACCOUNT NO.: 1428000-0109
DANVILLE LEASING
ACCOUNT NO.: 2046050-0100
DUNES LEASING
ACCOUNT NO.: 2392350-0103
FLINT CARTAGE
ACCOUNT NO.: 2797200-0103
GENESSE CARTAGE
ACCOUNT NO.: 3091400-0102
MCKINLAY TRANSPORT
ACCOUNT NO.: 5182300-0107
MICHIANA TRUCK
ACCOUNT NO.: 5314100-0108
MICHIGAN EXPRESS
ACCOUNT NO.: 5330700-0705
MOHAWK MOTOR
ACCOUNT NO.: 5558400-0200
QUAD STATE LEASING
ACCOUNT NO.: 6515675-0101

Appendix B

Dear Mr. Sigler:

Public Law 93-209, commonly called ERISA, requires us as the Fiduciary to make periodic reviews of participating employers contributions for the benefit of Plan Participants and their Beneficiaries.

We would like to make this review at your offices beginning the week of November 26, 1979 with a representative of Local Union No. 124.

This review will encompass the follows:

1. Determination of eligible Plan Participants covered by Collective Bargaining Agreements.
2. Verification of member history contributions.
3. Reconciliation of any account balances differences.

The records required will be the documents which support the recording of time worked and payroll computation and recording for all collective bargaining unit employees.

Our findings will be discussed with you at the completion of the review and confirmed in a written report.

If you have any further questions, please call your local Business Agent, or call Mr. John P. O'Sullivan at our toll-free number, (800) 323-2152, Extension 417.

Very truly yours,

(s) JACK YARBROUGH
ASSISTANT EXECUTIVE DIRECTOR

JY:JOP:jls

cc: Mr. John L. Sherry, Director, Financial Group
Mr. George Psaras, Director, Operations Accounting
Mr. Edward G. Lienhard, Manager, Delinquent Account/In-House Employer Audit
Mrs. Susie Mkrdichian, Manager, Accounts Receivable
Mr. John P. O'Sullivan, Manager, Field Employer Audit
Local Union Nos. 7, 20, 24, 34, 40, 100, 124, 135, 164, 299, 325, 332, 377, 406, 407, 414, 486, 527, 580, 614, 908 and 957

APPENDIX C
Title 26, Internal Revenue Code

§ 7601. Canvass of districts for taxable persons and objects

(a) General rule.—The Secretary or his delegate shall, to the extent he deems it practicable, cause officers or employees of the Treasury Department to proceed, from time to time, through each internal revenue district and inquire after and concerning all persons therein who may be liable to pay any internal revenue tax, and all persons owning or having the care and management of any objects with respect to which any tax is imposed.

(b) Penalties.—

For penalites applicable to forcible obstruction or hindrance of Treasury officers or employees in the performance of their duties, see section 7212.

Aug. 16, 1954, c. 736, 68A Stat. 901

§ 7602. Examination of books and witnesses

For the purpose of ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue tax or the liability at law or in equity of any transferee or fiduciary of any person in respect of any internal revenue tax, or collecting any such liability, the Secretary or his delegate is authorized—

(1) To examine any books, papers, records, or other data which may be relevant or material to such inquiry;

(2) To summon the person liable for tax or required to perform the act, or any officer of employee of such person, or any person having possession, custody, or care of books of account containing entries relating to the business of the person liable for tax or required to perform the act, or any other person the Secretary or his delegate may deem proper, to appear before the Secretary or his delegate at a time and place named in the summons and to produce such books, papers, records, or other data, and to give such testimony, under

oath, as may be relevant or material to such inquiry; and

(3) To take such testimony of the person concerned, under oath, as may be relevant or material to such inquiry.

Aug. 16, 1954, c. 736, 68A Stat. 901.